A Bad Tax, by Any Other Name

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The Hong Kong government recently announced its intention to introduce a lump sum levy of HK$9,600 on employers of foreign domestic helpers at the time the employment contract is approved, effective from October 1st. It further announced that it would reduce the minimum salary level of the helpers by HK$400 per month from April 1st. Over a standard two-year employment contract, this means that the lump sum employers’ levy is exactly equal to the total salary reduction. On the reasonable assumption that employers would reduce their employees’ wages to the new minimum, employers would thus carry no extra financial burden as a result of the new measures. This would fall entirely on the shoulders of the domestic helpers themselves.

The new levy was introduced under the labour importation scheme, thus technically is not government taxation, and so does not have to go through the legislative process that applies to changes in taxation. However, there should be no doubt as to what these measures in practice represent. No matter how they are dressed up, they are in all but name a tax on the salaries of domestic helpers. In this article, therefore, I shall refer to the measures as such – a new tax.

Since they were put forward, the government measures have attracted a significant amount of comment, both in favour and opposed. As I see it, three distinct but related main questions have been raised. First, there is the economic question as to whether any increase in government levies is appropriate at a time when Hong Kong is mired in recession. Second is the question of whether a reduction in the domestic helpers’ minimum salary is currently justified. And third is whether a “tax” on domestic helpers’ incomes is a just and appropriate way of alleviating the deficit.

As to the first of these questions, the technical arguments are complex and, as is usual in economics, a matter of heated debate. I will not add further to this particular debate here.

The second issue is whether a reduction in the domestic helpers’ minimum wage is currently justified. Several arguments in favour of a reduction have attracted wide political support, for example from the DAB and the HK Progressive Alliance. These arguments have varying degrees of persuasiveness. One of the least convincing is that in recent years the Hong Kong dollar, on the coat-tails of its US counterpart, has risen sharply against the peso, baht and ringgit, increasing the value of remittances to the Philippines, Thail and Indonesia, from where most domestic helpers come (the US dollar recently touched record highs against the peso, although falling against the yen and euro). Thus, it can be argued that a decrease in the minimum salaries of domestic helpers here is justified, since in terms of their own countries’ currencies, they have recently risen dramatically. The problem with this argument is that it is unusual, to say the least, for remuneration levels to be based on the personal home circumstances of the salary earner, rather than the actual quality or quantity of the work done. Further, little was heard of this argument when the US and HK dollars were falling against the above currencies. In any case, it ignores the effect of inflation in the home country, which in open economies tends to rise in tandem with falls in the exchange rate.

Another point often made in favour of a salary cut is that domestic helpers are privileged in that they represent the only sector of society to which a government-enforced minimum salary level applies. In their case, then, salary levels are therefore not set by the objective hand of market forces; rather they are set “by committee”. Consequently, so the argument runs, there is nothing sacred about the current minimum salary level of HK$3,670, and it should be adjusted as economic circumstances require. In the absence of this protection, so it is said, the salaries of domestic helpers would likely fall precipitously, and thus a statutory cut is now appropriate.

It is clear that deflation has been persistent in Hong Kong since the last minimum salary adjustment, also a decrease, of five percent in 1999. It is also fair to say that compared to minimum salary levels for domestic helpers elsewhere in the region, such as in Singapore and Malaysia, the level pertaining in Hong Kong is high. Arguments that the minimum salary is low compared to the Hong Kong average income are countered by the point that the comparison does not take into account other benefits that domestic helpers enjoy, such as free accommodation, health care, food, and travel expenses to and from their home country.

The contention that domestic helpers are currently treated favourably may thus have some appeal to many Hong Kong citizens. However, it ignores the reason why the minimum salary legislation was established in the first place. Given their position as guest workers, with their numbers regulated, and with their continued stay in Hong Kong subject to their continued employment, domestic helpers would, in the absence of such legislation, be open to exploitation by unscrupulous employers (some exploitation is clearly present in Hong Kong today in spite of its presence). It also ignores the long hours that most
domestic helpers are often expected to work to earn their incomes.

Nevertheless, there is, then, at least some justification for both views that the time is ripe for the budget deficit to be reduced and domestic helpers’ salary levels to be lowered. This then leads to the third question: whether it is appropriate to “kill two birds with one stone” by introducing a tax that adds to government revenues while reducing the domestic helpers’ incomes.

One argument often stated in favour of the “tax” on domestic helpers is that they create certain burdens on society that has to be paid for by taxpayers as a whole, and that thus the domestic helpers should shoulder some of the tax burden. In particular, domestic helpers are widely accused of creating an environmental problem in Central and other locations where they congregate on their days off.

There is no doubt that anti-social littering constitutes a serious and costly problem for Hong Kong, and that at certain times of the week and in certain places, domestic helpers clearly contribute to this problem (somewhat ironically it has to be said, since they are in Hong Kong primarily to perform cleaning tasks). “Making the polluter pay” is a principle that is gaining currency throughout the world as a response to a variety of ecological concerns. Taxation is an effective, and widespread, means of putting this principle into effect, and so one might well sympathise with calls for a tax on the guilty parties to pay for the clean-up. However, the problem is one of fairness in applying the tax; it should fall on all the miscreants. One has only to witness beaches, barbecue areas and other public areas all over Hong Kong to understand that the failure to deposit rubbish in the proper receptacles hardly applies solely to the overseas domestic helper community. Thus, to tax that section of society alone would clearly be unfair.

This is a comparatively petty point, however. The main argument put forward in favour of the tax is that in order to reduce the ballooning budget deficit, every member of society should play his or her part (this phrase has been a constant refrain of government). It is, at first glance, a laudable objective. The new levy will of course raise extra government revenue – with 240,000 overseas helpers currently in Hong Kong, the levy would generate over one billion dollars per annum in extra revenue. Thus the domestic helpers would no doubt be “playing their part”. The problem with this argument is that in Hong Kong every member of society clearly does not play his or her part. Far from it: in the tax year 2000/1, according to the IRD’s recently released annual report, there were only 1.2 million salaries taxpayers in the territory, out of a combined workforce of approximately two-and-a-half times that figure. Due to the current level of personal allowances, which are very high by international standards, most income earners in Hong Kong do not pay any tax whatsoever, and this will continue to be the case in spite of the lowered allowances proposed in the recent budget.

So, here has been the government’s dilemma. In order to tax the domestic helpers under the existing tax structure, personal allowances would have to be dramatically reduced and progressive tax rates substantially raised, an option that the government could not find politically or economically feasible. Thus, the solution has been to “tax” the helpers under a different system, meaning the introduction of the new levy on employers, effectively Hong Kong’s first payroll tax.

Under the new measures, domestic helpers stand to be taxed at an effective rate of approximately ten and a half percent of their income, a rate not suffered by other single-person salary earners until they earn more than $34,000 a month, or over ten times the helpers’ revised income. The new “tax” thus clearly violates the principle of equity, which has been accepted as one of the basic tests of a good tax system since they were outlined over two hundred years ago by Adam Smith in his seminal work The Wealth of Nations. It is also taxation without the merest hint of representation, since domestic helpers, as guest workers in the territory, have no political voice in Hong Kong. Further, it targets workers who are both foreign and overwhelmingly female, and thus can be accused of being discriminatory on the basis of both nationality and sex. As such, it is in breach of the International Covenant on Civil and Political Rights, enshrined in Hong Kong’s own Basic Law. No matter what justification there is for it in terms of revenue and in terms of realigning salary levels, it is a bad “tax”, by any other name, and should have no part to play in the finances of a society that has aspirations of calling itself a “world city”.

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