

**Commission on Strategic Development
Committee on Governance and Political Development**

Provisions in the Basic Law concerning the Capitalist Economy

Introduction

At the first meeting of the Committee, Members discussed how we could effectively ensure that the various Basic Law principles could be fully implemented in the process of constitutional development and when the ultimate aim of universal suffrage is attained. These principles include facilitating the development of the capitalist economy and meeting the interests of different sectors of society, so as to maintain the stability and prosperity of Hong Kong.

2. This paper aims at providing background information on the Basic Law provisions concerning the capitalist economy to facilitate members' discussion on the subject.

Guiding principles for designing the electoral system

3. According to the Preamble of the Basic Law, the basic policies of the State regarding the Hong Kong Special Administrative Region ("HKSAR") are that to maintain the prosperity and stability of Hong Kong, and to take account of its history and realities, the State has decided that a HKSAR will be established, and that under the principle of "One Country, Two Systems", the socialist system and policies will not be practised in Hong Kong.

4. In submitting the Basic Law (Draft) and related documents at the Third Session of the Seventh National People's Congress (NPC) on 28 March 1990, Director Ji Pengfei made the following explanation:

"The political structure of the HKSAR should accord with the principle of 'One Country, Two Systems' and aim to maintain stability and prosperity in Hong Kong in line with its legal status and actual situation. To this end, consideration must be given to the interests of the different sectors of society and the structure must facilitate the development of the capitalist economy in the Region. While the part of the existing political structure proven to be effective

will be maintained, a democratic system that suits Hong Kong's reality should gradually be introduced.”

5. From the above explanation, it can be seen that in designing a universal suffrage system for electing the Chief Executive and for forming the Legislative Council (LegCo), consideration must be given to how it could contribute to Hong Kong's prosperity and stability, facilitate the development of its capitalist economy, and meet the interests of different sectors of society. This guiding principle is embodied in the provisions of the Basic Law.

Provisions in the Basic Law concerning the capitalist economy

6. The General Principles of the Basic Law (Chapter 1) provide for the fundamental principles on the systems and policies to be practised in the HKSAR. Before Reunification, Hong Kong was already an important international trade and financial centre. To preserve the prosperity of Hong Kong, it is necessary to maintain its previous capitalist system. Article 5 of the Basic Law provides that “the socialist system and policies shall not be practised in the HKSAR, and the previous capitalist system and way of life shall remain unchanged for 50 years.” As the foundation of a capitalist economy is a system of private ownership of property, Article 6 of the Basic Law stipulates that “the HKSAR shall protect the right of private ownership of property in accordance with law.”^{Note 1}

7. The various specific economic systems are prescribed in Chapter V of the Basic Law, which provide guiding principles for the economy of the HKSAR. The provisions deal with the following areas.

Independent financial system

8. Article 106 of the Basic Law stipulates that “the HKSAR shall have independent finances.” The finances of the HKSAR are not incorporated into the finances of the State, but are managed by the SAR Government on its own. However, when drawing up its budget on its own, the SAR Government shall follow the fiscal principles laid down in the Basic Law.

9. Article 107 of the Basic law stipulates that “the HKSAR shall follow the principle of keeping expenditure within the limits of revenues in drawing up its budget, and strive to achieve a fiscal balance, avoid deficits and keep the

^{Note 1} Wang Shuwen (ed.), *Introduction to the Basic Law of the Hong Kong Special Administrative Region*, p.327

budget commensurate with the growth rate of its gross domestic product.” This provision is based on Hong Kong’s successful experience in the past, and aims at maintaining the long-term prosperity and stability of the HKSAR. According to the analysis in *Introduction to the Basic Law of the Hong Kong Special Administrative Region* by Wang Shuwen (ed.),^{Note 2} the rationale behind this provision is as follows.

- (a) When drawing up a budget, the principle of keeping expenditures within the limits of revenues shall be followed. If expenditures are allowed to increase without regard to revenues, a deficit is bound to occur, or the HKSAR will need to increase taxes, obtain foreign loans, issue government bonds in the Region or increase money supply to defray its expenditures. This will only lead to financial difficulty, resulting in economic crisis.
- (b) Efforts should be made to achieve a fiscal balance and avoid deficits. To keep expenditures within the limits of revenues, a basic balance between revenues and expenditures should be maintained. This is a prudent financial policy. If expenditures, such as welfare expenditures, are greatly increased to attain a certain aim, it would not be a long-term solution even if the welfare level of the community could be temporarily raised.
- (c) The growth rate of revenues and expenditures should be commensurate with the growth rate of gross domestic product, that is, they should not, in principle, exceed or greatly exceed the growth rate of production. Gross domestic product is an indicator of the level of wealth. An increase in gross domestic product represents an increase in production in the economy. Only when the government increases its revenues and expenditures on the basis of enhanced production can such an increase be considered solid.

10. Wang Shuwen also stated in the same article that the three points mentioned above are not mechanical, applying only to a certain fiscal year or a certain short period of time. In a given fiscal year or a given short period of time, there may be exceptional circumstances, or extraordinary measures may have to be in place for some specific reasons. However, in the long run, the three points above are crucial to maintaining a stable economy.

^{Note 2} Wang Shuwen (ed.), *Introduction to the Basic Law of the Hong Kong Special Administrative Region*, p.566.

Independent Taxation

11. In accordance with Article 108 of the Basic Law, “The HKSAR shall practise an independent taxation system. The HKSAR shall, taking the low tax policy previously pursued in Hong Kong as reference, enact laws on its own concerning types of taxes, tax rates, tax reductions, allowances and exemptions, and other matters of taxation.” This provision has regard to the fact that the relatively low tax system adopted by Hong Kong has helped attract overseas and local investments, and has contributed to Hong Kong’s continuous stability and prosperity.

Maintaining a Private Ownership Economy

12. Under the principle of “One Country, Two Systems”, the Basic Law stipulates that Hong Kong shall remain a private ownership economy. Apart from Article 6 (see paragraph 6 above), Article 105 provides that “The HKSAR shall, in accordance with law, protect the right of individuals and legal persons to the acquisition, use, disposal and inheritance of property and their right to compensation for lawful deprivation of their property.”

Others

13. Apart from the financial and taxation systems, Chapter V of the Basic Law also contains provisions on monetary affairs, trade, industry and commerce, land leases, shipping and civil aviation. Director Ji Pengfei pointed out in his Explanation of the Basic Law (Draft) that these provisions were indispensable to ensuring the normal operation of Hong Kong’s capitalist economy and maintaining its status as an international financial centre and a free port.

Provisions of the Basic Law on Meeting the Interests of Different Sectors of Society

14. It is stated in Paper CSD/GC/1/2005 submitted for the first meeting that, as can be seen from the history of Hong Kong’s economic development, economic prosperity is largely dependent on the joint efforts of the industrial and business sectors, the middle class, professionals, the working class, and other sectors of society. To achieve the aim of maintaining prosperity and stability, we must deal with properly the issue of meeting the interests of different sectors. In accordance with this principle and having regard to the actual situation at that

time, Annex II to the Basic Law stipulates that half of the seats in LegCo would be returned by functional constituencies from its first to third terms.^{Note 3} In his statement, Director JI cited the voting procedures in LegCo stipulated in Annex II to the Basic Law as an example of meeting the interests of different sectors of society.

15. In accordance with the Decision of the Standing Committee of NPC (NPCSC) of 26 April 2004 on the methods for selecting the CE in 2007 and for forming the LegCo in 2008, the two methods shall be specified in the light of the actual situation in the HKSAR and in accordance with the principle of gradual and orderly progress, with universal suffrage as the ultimate aim. The Decision also states that any change relating to the two methods “shall conform to principles such as being compatible with the social, economic, political development of Hong Kong, being conducive to the balanced participation of all sectors and groups of the society, being conducive to the effective operation of the executive-led system, being conducive to the maintenance of the long-term prosperity and stability of Hong Kong.”

Conclusion

16. It can be seen from the above that, under the principle of “One Country, Two Systems”, we must ensure that, in the process of attaining the ultimate aim of universal suffrage and in designing a model for implementing universal suffrage, the above principles can be fully implemented, facilitating the development of the capitalist economy and meeting the interests of different sectors of society.

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^{Note 3} The “Decision” of the NPCSC of 26 April 2004 stipulates that the ratio between members returned by functional constituencies and members returned by geographical constituencies through direct elections, who shall respectively occupy half of the seats, is to remain unchanged in the fourth term of the Legislative Council.