

By hand & by fax (2869-6794)  
(Attn: Ms Rosalind Ma)

29 November 2000

Clerk to Bills Committee on Inland Revenue (Amendment) Bill 2000  
Legislative Council Secretariat  
3/F Citibank Tower  
3 Garden Road  
Central  
Hong Kong

Dear Sirs

Submission of Comments on Inland Revenue (Amendment) Bill 2000

We refer to our submission dated 20 November 2000 and your invitation to our Association for making an oral representation to the Bills Committee on 4 December 2000.

Taking the opportunities of the oral representation, we wish to include an additional submission point and enclose, as an attachment to this letter, our full representation in writing.

You will note that the original submission point (3) is now renamed as point (4) and a new point (3) is added.

For and on behalf of  
Association of Chartered Certified Accountants

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The Association of Chartered Certified Accountants 英國特許公認會計師公會

Jimmy Chung  
Chairman  
Budget and Tax Subcommittee  
of the Executive Committee 2000-01

cc Secretary for the Treasury, Ms Denise Yue, JP  
Commissioner of Inland Revenue Department, Mr Elmo D'Souza,  
JP

Submission to Bills Committee on  
**Inland Revenue (Amendment) Bill 2000**

On behalf of ACCA Hong Kong, we make the following submission relating to the above bill:

(1) Proposed Section 15(1)(ba) - The proposed amendment specifically provides that a sum for the use of intellectual properties outside of Hong Kong is deemed to be chargeable to Hong Kong tax if the sum is a deductible expense of a Hong Kong taxpayer.

Our comments: The proposal has altered our traditional territorial concept of taxation. Also, it creates uncertainty and complication in those situations where the taxpayers are entitled to offshore income claim and as such a part or whole of the expenses relating to the use of intellectual properties are non-deductible.

It is not clear, under such a scenario, whether the expenses attributable to offshore income are regarded as non-deductible or merely excluded from the calculation of assessable profits as a concession (particularly in the case of 50/50 claim for PRC processing arrangement) and, in consequence, whether the expenses are within the scope of Section 15(1)(ba).

(2) Proposed S16(2)(e)(D) - The proposed amendment shall disallow interest expense deduction on any borrowing specific for the acquisition of plant and machinery or trading stock where the borrowing is, directly or indirectly and in part or whole, secured by a non-taxable deposit or loan.

Our comments: The proposal ignores the commercial practice that banks generally require a line (L/C or T/R) be secured by an acceptable form of securities. Cash deposits rank probably as the most acceptable. To disallow the interest expense deduction would result in additional business cost to the taxpayers.

If banks are to accept other forms of securities, the credit risk may increase (which the Monetary Authority may not prefer) or the line to the taxpayer may be reduced (and this would negatively impact the overall business growth and economies)

- (3) Proposed S16(2)(f)(A),(B) & (C) - The proposed amendment shall disallow interest expense deduction arising from listed debentures or marketing instruments where for any particular issue one of the holders [of the debentures or instruments] is the borrower or associated with the borrower.

Our comments: The proposal ignores the fact that most of the issues are for genuine fund raising and that for financial management purpose either the issuer or an associated person may from time to time acquire part of the issue when

- (i) it is cheaper to borrow from the market instead of paying interest at the rate pre-determined by the issue; or
- (ii) there is a perceived need of using the instruments to secure ownership control of the issuer or an associated company.

By requiring all holders to be non-associated person (penalising associated person from holding the financial instrument), the amendment discourages sound financial management in that it will:

- (a) result, unnecessarily, in the disallowance of that part of the interest payable to non-associated holders;
- (b) remove the flexibility which may otherwise be available to the borrower or an associated person to hold the acquired instruments for reselling in the secondary market [when interest rate has changed] or securing control over the issuer or the borrower through a conversion right [as many of the instruments are convertible into equity]. The conversion right is particularly useful for protection against equity dilution.

We recommend that allowance should be granted to that part of the interest attributable to holdings by third parties.

- (4) Proposed amendment on Section 26E - the proposed amendment shall allow home loan interest deduction be extended to car parking space which is not valued together with a dwelling.

Our comments: The proposed amendment is welcomed. We note that the amendment, if passed, will apply with effect from assessment year 1998/99. We consider that this should not be used as a precedent for making retroactive amendments in the future.

While on Section 26E, we would point out that taxpayers generally find this part of the legislation difficult to comprehend and often they find too much unnecessary limitations in the application with the result that part of the deduction entitlement of a year may be lost.

We hope that our comments will be taken into consideration when hearing of the Amendment Bill is re-adjourned.