

Capital Markets Tax Committee Of Asia
Hong Kong Chapter

Your Ref: CB1/BC/1/00

26 March 2004

Mr Matthew Loo
for Clerk to Bills Committee
Legislative Council
Legislative Council Building
8 Jackson Road
Central, Hong Kong

Dear Mr Loo

Bills Committee on Inland Revenue (Amendment) Bill 2000

Thank you for your letter of 3 March 2004 allowing us the opportunity to submit our views below on the scope of the proposed exemption for market making activities.

By copy of this letter, we would also like to thank the Inland Revenue Department (the "IRD") for their understanding and agreement to exempt market making activities from the operation of the proposed restriction on interest deduction.

Market making ordinarily involves putting oneself out as a willing buyer or seller through making available buy-sell prices to the public on a continuous basis typically via a financial information service such as Bloomberg, Reuters, etc. The market-maker is obligated to buying or selling at those published prices. In major markets such as the U.S. and U.K., this is an activity regulated under securities laws and must be carried out by authorised dealers or brokers. In Hong Kong, "dealing in securities" is a regulated activity under the Securities and Futures Ordinance (the "SFO") and its definition is rather wide. It includes making or inducing another person to enter into an agreement to acquire, dispose of, subscribe or underwrite securities. A person who carries on, or holds himself as carrying on, a business in a regulated activity has to be either exempted or authorised under the SFO, and has a substantial capital base to support its buy-sell commitments. While it is not entirely clear, market making in Hong Kong may be regarded as "dealing in securities" falling under the regulatory regime of the SFO. As such, market making activities are typically carried out by dealers or brokers. It is extremely unlikely that other persons such as controlling shareholders or directors of a company would engage in market making.

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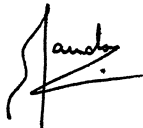
A market maker would at all normal times hold himself out as willing to buy or sell on a continuous basis the securities for which they act as a market maker. Otherwise, it would defeat the purpose of providing liquidity in the securities. This must be distinguished from purchases or sales of securities by any persons for various commercial reasons at only selective times.

We note and understand the IRD's concerns that the proposed exemption for market making may be abused for tax avoidance purposes. The restriction of the exemption to activities by market makers in their ordinary course of the business of market making would, we believe, mitigate the risk of an abuse.

Given the above, we believe that the scope of the exemption for market making as it currently stands in the draft bill is sufficient to cover genuine market making activities and would also address the IRD's concerns of the risk of an abuse.

Should you wish to discuss the above further, please contact David Sutherland on 2848 6801 or myself on 2536 3496.

Yours sincerely



Jean-Pierre Baudoux
Chairman

cc Mr Patrick Tam, Inland Revenue Department