

LEGISLATIVE COUNCIL BRIEF

Inland Revenue Ordinance
(Cap.112)

EXEMPTION FROM SALARIES TAX (INTERNATIONAL FINANCE CORPORATION) ORDER

INTRODUCTION

At the meeting of the Executive Council on 22 May 2007, the Council ADVISED and the Chief Executive ORDERED that the Exemption from Salaries Tax (International Finance Corporation) Order (“the Order”) at Annex should be made. The Order seeks to exempt any Chinese national or permanent resident of the Hong Kong Special Administrative Region (HKSAR) who is employed by or holding an office in the International Finance Corporation (IFC) from payment of salaries tax chargeable under section 8 of the Inland Revenue Ordinance (Cap.112) (IRO).

JUSTIFICATIONS

IFC’s Request

2. IFC’s office in Hong Kong was opened in September 2000. The issue of salaries tax exemption for Chinese staff was discussed at that time with no agreement reached since the Central People’s Government (CPG) did not consider that it was its international obligation to provide salaries tax exemption to Chinese nationals working for IFC on the Mainland.

3. Since the opening of the Hong Kong office, IFC has been hiring Chinese nationals to work in the Hong Kong office indirectly through employment agencies. IFC reopened the issue with the CPG in 2005 arguing that the Hong Kong office had experienced increasing difficulties in recruiting and retaining high-quality Chinese staff. Because of the absence of salaries tax exemption, IFC was also unable to send Chinese nationals employed by the World Bank Group elsewhere to work in Hong Kong as the staff would have to forego the tax exemption they were enjoying in other overseas offices. The CPG considered that it would be a matter for the HKSAR Government to

decide on the proposed tax exemption under Article 108 of the Basic Law¹.

4. In September 2006, IFC informed the Hong Kong Monetary Authority about its management's intention to combine the regional functions of its Asian offices to form one single Asia hub.² IFC further indicated that consideration was being given to locating the combined Asia hub in Hong Kong or other cities in Asia, and the granting of salaries tax exemption for IFC local staff would be of critical importance to its continued presence in Hong Kong.

Relevant Considerations

5. The Administration has taken into account the following factors in considering IFC's request for salaries tax exemption –

- (a) IFC's continued presence and expansion would bring benefits to Hong Kong. IFC's mission is to promote private sector investment in developing countries. Its annual investments in the Asia-Pacific region have tripled to approach US\$1 billion in 2006 since the opening of its Hong Kong office in 2000. In addition, IFC has been playing a catalytic role in promoting bond market development in the region. It has issued more than HK\$22 billion of high-quality Hong Kong dollar debt securities in Hong Kong over the years. It is also one of the three foreign financial institutions approved by the Ministry of Finance in 2004 to issue renminbi "panda bonds" on the Mainland. While Hong Kong may not be a target destination of IFC's investment, its presence here will be a vote of confidence in Hong Kong's political and economic stability. It is also an endorsement of our status as an international financial centre. If IFC decides to relocate out of Hong Kong, we envisage that other places in the region which aspire to be international financial centres would readily offer to house IFC's regional office. If IFC's Hong Kong office is closed and relocated elsewhere, our reputation and status as an international financial centre would be affected.

¹ Basic Law Article 108: 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.

² IFC currently maintains seven regional offices worldwide. IFC's latest plan is to further decentralize its management at headquarters and reorganize these regional offices to form three regional hubs worldwide including one for Asia.

- (b) Currently, IFC has offices in 62 countries. According to IFC's information, almost all hosting jurisdictions have granted tax exemption to all IFC's local staff. Therefore, the granting of salaries tax exemption to IFC's local staff in Hong Kong is generally in line with this international practice.
- (c) IFC indicated that it was difficult to recruit and retain quality Chinese staff. It could not send Chinese staff working in other offices to work here as those staff would have to forego the tax exemption they were enjoying in other offices. The granting of salaries tax exemption would facilitate IFC's recruitment of both Mainland Chinese and Hong Kong permanent residents to work in the Hong Kong office. This would encourage more Chinese nationals and Hong Kong permanent residents to take up the professional and senior management positions at the Hong Kong office and gain greater prominence in the World Bank Group. As at end 2006, there were 54 staff in the IFC's office in Hong Kong (20 of them were hired through employment agencies). It is expected that the expanded office will have as many as 95 staff by mid-2008.

OTHER OPTIONS

6. The requested tax exemption has to be granted through legislative means. It cannot be effected through administrative arrangement.

THE ORDER

7. Section 87 of the IRO provides that the Chief Executive in Council may, by order, exempt any person, office or institution from payment of the whole or any portion of any tax chargeable under the Ordinance.

8. The Order made under section 87 of the IRO seeks to exempt any Chinese national or HKSAR permanent resident who is employed by or holding an office in IFC from payment of salaries tax chargeable under section 8 of the IRO.

LEGISLATIVE TIMETABLE

9. The legislative timetable will be –

Publication in the Gazette	1 June 2007
Tabling in the Legislative Council	6 June 2007
Completion of negative vetting	The first Legislative Council meeting of the 2007/08 session
Commencement	The third day after the completion of the negative vetting

IMPLICATIONS OF THE PROPOSAL

10. The granting of the requested tax exemption to IFC is in conformity with the Basic Law, including the provisions concerning human rights. The grant of the exemption will not affect the binding effect of the existing provisions of the Ordinance and its subsidiary legislation.

11. The accession to IFC's request would help induce IFC to retain and expand its office in Hong Kong. Given the importance of IFC in the international arena, its presence would help uphold the image of Hong Kong as an international financial centre, and also bring about increased financial activities to the benefit of the Hong Kong economy. The granting of the requested tax exemption will not give rise to any productivity, environmental, civil service or sustainability implications. The financial implications arising from the grant of the tax exemption should be minimal.

PUBLIC CONSULTATION

12. No public consultation has been conducted on the matter.

PUBLICITY

13. A press release will be issued. A spokesman will answer media and public enquiries.

BACKGROUND

14. IFC is one of the member institutions of the World Bank Group, which aims to reduce poverty. It is a United Nations Specialized Agency. IFC was set up in 1956 to promote sustainable private sector

development in developing countries by promoting development of capital markets and productive enterprises.

15. IFC opened a joint office with the International Bank for Reconstruction and Development (IBRD) in Hong Kong in September 2000 under a Memorandum of Understanding signed between the CPG, IFC and IBRD. The Memorandum, IFC's Articles of Agreement and the United Nations Convention on the Privileges and Immunities of the Specialized Agencies provide for certain privileges and immunities to be granted to IFC and its regional office in Hong Kong.

ENQUIRIES

16. Enquiries on this brief can be directed to Ms Angelina Kwan, Principal Assistant Secretary for Financial Services and the Treasury (Financial Services) at 2529 0121.

Financial Services and the Treasury Bureau
1 June 2007

L.N. 101 of 2007

**EXEMPTION FROM SALARIES TAX (INTERNATIONAL
FINANCE CORPORATION) ORDER**

(Made by the Chief Executive in Council under section 87 of the
Inland Revenue Ordinance (Cap. 112))

1. Commencement

This Order shall come into operation on 13 October 2007.

2. Interpretation

In this Order—

“International Finance Corporation” (國際金融公司) means the international organization of that name established in Washington, D.C. on 24 July 1956.

3. Exemption from salaries tax

(1) A Chinese national or Hong Kong permanent resident is exempt from the payment of salaries tax chargeable under section 8 of the Ordinance in respect of his income—

(a) arising in or derived from Hong Kong from—

- (i) his holding an office in the International Finance Corporation; or
- (ii) his employment with the International Finance Corporation; and

(b) paid by the International Finance Corporation.

(2) This section applies in relation to salaries tax chargeable for the year of assessment commencing on 1 April 2007 and for all subsequent years of assessment.

LAM Chik-ting, Tony
Clerk to the Executive Council

COUNCIL CHAMBER
22 May 2007

Explanatory Note

This Order exempts Chinese nationals and Hong Kong permanent residents employed by, or holding an office in, the International Finance Corporation from the payment of salaries tax chargeable under section 8 of the Inland Revenue Ordinance (Cap. 112) in respect of their income from the International Finance Corporation.