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Proposal to Attract Enterprises to Establish Corporate Treasury Centres (“CTCs”) in Hong Kong

LegCo Panel on Financial Affairs

Meeting on 1 June 2015

2015-16 Budget

- To attract multinational and Mainland enterprises to establish CTCs in Hong Kong to perform treasury services for their group companies, the Financial Secretary announced that the Government would amend the Inland Revenue Ordinance (“IRO”, Cap. 112) to–
  - allow, under specified conditions, interest deductions under profits tax for CTCs
  - reduce the profits tax for specified treasury activities by 50%

CTC

- An "in-house bank" within a multinational corporation ("MNCs") focusing on the optimal procurement and usage of capital for the operations of the entire group

- Objectives:
  - lower transaction cost
  - improve corporate efficiency

- Typical functions:
  - intra-group borrowing and lending of money
  - optimising multi-currency cash management and liquidity management
  - central or regional processing of payments to vendors or suppliers for the corporate group
  - conducting transactions for financial or treasury-related risk management
  - supporting the raising of capital by the group

Justifications

- Hong Kong is Asia’s premier location for CTCs

- If more CTCs are established in Hong Kong-
  - create demands for financial and professional services sectors
  - contribute to the development of headquarters economy

Issues

- Interest deduction rules
  - Relatively less favourable for MNCs to engage in intra-group borrowing and lending of funds
    - Interest expense payable to associated corporations outside Hong Kong are not tax deductible, whereas the interest income arising from its business of the borrowing from and lending of money to associated corporations in or outside Hong Kong is chargeable to profits tax
- Fierce competition in the region
  - Some markets have introduced tax incentives

Legislative proposal

- Deduction of interest expense
- Concessionary tax rate for qualifying CTCs

Deduction of interest expense

- Allow deduction of interest expenses if a corporation borrows from associated corporations outside Hong Kong in the ordinary course of the business of the borrowing from and lending of money to associated corporations in or outside Hong Kong
  - Condition: the corresponding interest received by the associated corporation is subject to tax of substantially the same nature of profits tax in a territory outside Hong Kong with the tax paid thereon at a rate not lower than the Hong Kong's profits tax rate

- Make it clear that interest income and specified disposal profits earned by a corporation, in respect of the business of the borrowing from and lending of money to associated corporations in or outside Hong Kong, are deemed trading receipts chargeable to profits tax

Concessionary tax rate for qualifying CTCs

- Standalone regime for qualifying CTCs in the IRO

- 50% of the profits tax rate (i.e. 8.25%) applies to qualifying profits of a qualifying CTC-
  - Loans made to associated corporations outside Hong Kong
  - Qualifying corporate treasury services for associated corporations outside Hong Kong
  - Qualifying corporate treasury transactions undertaken on its own account with any person not carrying on a trade, profession or business in Hong Kong

Concessionary tax rate for qualifying CTCs

- Need to ensure that a company is genuinely carrying on CTC business, and the half-rate applies only to qualifying profits but not other non-CTC income.

- Entity-based approach
  - a group company which elects to enjoy the half-rate should dedicatedly, via a standalone corporate entity-
    - carry on the intra-group borrowing and lending business
    - perform “qualifying corporate treasury services”
    - enter into “qualifying corporate treasury transactions” on own account

Concessionary tax rate for qualifying CTCs

- “Safe harbour rules”
  - To provide operational flexibility for CTCs with other non-CTC income and assets

- Anti-avoidance provisions
  - Half-rate will apply to assessable profits in respect of which the corresponding payments made are not tax deductible in Hong Kong

Way forward

- Engaging the treasury industry and other interested parties on a Bill to implement the proposal
- Introduce the Bill into LegCo during 2015-16 legislative session