

LEGISLATIVE COUNCIL BRIEF

Inland Revenue Ordinance
(Chapter 112)

EXEMPTION FROM PROFITS TAX (NON-RENMINBI SOVEREIGN BONDS) ORDER

INTRODUCTION

At the meeting of the Executive Council on 28 November 2017, the Executive Council **ADVISED** and the Chief Executive **ORDERED** to make the Exemption from Profits Tax (Non-Renminbi Sovereign Bonds) Order (“the Exemption Order”) at **Annex** pursuant to section 87 of the Inland Revenue Ordinance (Cap. 112) (“IRO”) to exempt a person from the payment of profits tax chargeable under Part 4 of the IRO in respect of sums received by or accrued to the person as interest paid or payable on, or profits on the sale or other disposal or on the redemption on maturity or presentment of, sovereign bonds denominated in currencies other than Renminbi (“RMB”) issued in Hong Kong by the Central People’s Government (“CPG”).

JUSTIFICATIONS

2. Having regard to the justifications set out in paragraphs 3 to 5 below, we consider it appropriate that profits tax exemption¹ available to RMB sovereign bonds should be extended to cover non-RMB (including

¹ Pursuant to the Exemption from Profits Tax (Renminbi Sovereign Bonds) Order (Cap. 112BH) made by the CE-in-C in 2009 under section 87 of the IRO, a person is exempt from the payment of profits tax chargeable under Part 4 of the IRO in respect of sums received by or accrued to the person as interest paid or payable on, or profits on the sale or other disposal or on the redemption on maturity or presentment of, RMB sovereign bonds issued in Hong Kong by the CPG.

US dollar (“USD”)) denominated sovereign bonds issued in Hong Kong by the CPG.

3. Following the first issuance of RMB sovereign bonds by the CPG in Hong Kong in 2009, the Exemption from Profits Tax (Renminbi Sovereign Bonds) Order (Cap. 112BH) was made to promote further issuances of RMB sovereign bonds in Hong Kong by the CPG on an on-going and regular basis with a view to strengthening our role as a testing ground for policy measures for diversification of RMB business and upholding our position as an international financial centre. We consider that the extension of profits tax exemption to non-RMB denominated sovereign bonds aligns with these policy objectives.

4. The issuance of USD denominated sovereign bonds in Hong Kong by the CPG in 2017 is the first of this sort after Hong Kong’s return to the motherland². It provides a stable and sound investment option for local and international investors, thereby expanding the base of bond investors in Hong Kong. It will also be beneficial to the development of financial services in Hong Kong through increasing the breadth and depth of the local bond market and enhancing financial cooperation between the Mainland and Hong Kong.

5. The issuance of USD denominated sovereign bonds in Hong Kong signifies the CPG’s efforts in diversifying Mainland’s debt structure and promoting overseas investors’ participation in the Mainland’s bond market in the future. It could also serve as a channel for the CPG to showcase (e.g. through roadshows) the Mainland’s latest developments on various fronts and instil confidence in international investors, which will in turn help accelerate the internationalisation of RMB. Against such backdrop, the Exemption Order will help ensure that Hong Kong continues to be the premier platform facilitating the internationalisation of RMB and the Mainland to “go global” by maintaining Hong Kong’s competitiveness and attractiveness as the preferred location for the CPG to issue sovereign bonds regardless of the currencies denominated.

² The CPG issued USD denominated sovereign bonds amounted to USD 300 million in Hong Kong in 1993.

THE EXEMPTION ORDER

6. 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 IRO. The Exemption Order exempts a person from the payment of profits tax chargeable under Part 4 of the IRO in respect of sums received by or accrued to the person as interest paid or payable on, or profits on the sale or other disposal or on the redemption on maturity or presentment of, non-RMB (including USD) denominated sovereign bonds issued in Hong Kong by the CPG, so that the relevant tax arrangement is on par with that applicable to RMB sovereign bonds issued in Hong Kong by the CPG.

7. The Exemption Order covers sovereign bonds issued in Hong Kong by the CPG in all currencies (other than RMB) considering that the CPG may in future issue sovereign bonds in currencies other than RMB or USD. As the Ministry of Finance (“MoF”) has issued the USD denominated sovereign bonds in Hong Kong on 26 October 2017 (i.e. in the year of assessment commencing 1 April 2017), the Exemption Order shall apply to the year of assessment commencing on 1 April 2017 and for all subsequent years of assessment.

LEGISLATIVE TIMETABLE

8. The legislative timetable is as follows –

Publication in the Gazette	12 January 2018
Tabling at Legislative Council (“LegCo”)	17 January 2018
Commencement date	30 March 2018

IMPLICATIONS OF THE PROPOSAL

9. The proposal is in conformity with the Basic Law, including the provisions concerning human rights. It will not affect the binding effect

of the existing provisions of the IRO. There are no productivity, environmental, family, gender and civil service implications. Apart from the economic implications in paragraph 10 below, there are no other sustainability implications.

10. On economic implications, the Exemption Order will facilitate the CPG's issuance of USD denominated sovereign bonds in Hong Kong and is conducive to the further development of our bond market. It will also help strengthen financial cooperation between Hong Kong and the Mainland, thereby strengthening our position as an international financial centre.

11. On financial implications, on the basis that the coupon rates for the USD 1 billion 5-year sovereign bonds and USD 1 billion 10-year sovereign bonds are 2.125% and 2.625% respectively, the estimated amount of tax foregone following the implementation of the Exemption Order would be around HK\$ 60.95 million each year in the first five years. Upon expiry of the 5-year bonds, the tax foregone for the sixth to tenth years would be reduced to HK\$ 33.68 million each year. The above estimation only includes profits arising from interest payment. No revenue foregone could be estimated for profits on the sale, other disposal, and redemption on maturity or presentation of the bonds as there is no basis to make this projection.

PUBLIC CONSULTATION

12. In the Government's press release welcoming MoF's issuance of the USD denominated sovereign bonds in Hong Kong issued on 11 October 2017, we mentioned that we would study extending the scope of the profits tax exemption to cover non-RMB (including USD) denominated sovereign bonds issued in Hong Kong by the CPG. We also issued an information note to the LegCo Panel on Financial Affairs on 12 January 2018.

PUBLICITY

13. We shall arrange a spokesperson to deal with press enquiries on the Exemption Order.

BACKGROUND

14. The CPG, through the MoF, has since 2009 issued RMB sovereign bonds in Hong Kong every year. The annual total amount of RMB sovereign bonds issued in Hong Kong between 2009 and 2014 had been on the rising trend. Since then, the total amount has been maintained at RMB 28 billion per annum. However, in June 2017, the MoF announced its plan to issue RMB sovereign bonds totalling RMB 14 billion in Hong Kong (a reduction by half as compared to that in 2016) and to issue USD denominated sovereign bonds outside the Mainland totalling USD 2 billion (roughly equivalent to RMB 14 billion) in the second half of 2017. On 11 October 2017, the MoF announced that it would issue USD denominated sovereign bonds totalling USD 2 billion in Hong Kong, of which USD 1 billion would be issued in 5-year tenor and the remaining USD 1 billion in 10-year tenor. The issuance was completed on 26 October 2017.

ENQUIRIES

15. Enquiries on this brief may be directed to Ms Estrella Cheung, Principal Assistant Secretary for Financial Services and the Treasury (Financial Services), at 2810 2150.

Financial Services and the Treasury Bureau
12 January 2018

Exemption from Profits Tax (Non-Renminbi Sovereign Bonds) Order

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

1. Commencement

This Order comes into operation on 30 March 2018.

2. Interpretation

In this Order—

non-Renminbi sovereign bonds (非人民幣國債) means bonds—

- (a) denominated in any currency other than the Renminbi; and
- (b) issued in Hong Kong by the Central People's Government.

3. Exemption

- (1) A person is exempt from the payment of profits tax chargeable under Part 4 of the Ordinance in respect of sums received by, or accrued to, the person as—
 - (a) interest paid or payable on non-Renminbi sovereign bonds;
 - (b) profits on the sale, or other disposal, of non-Renminbi sovereign bonds; or
 - (c) profits on the redemption, on maturity or presentment, of non-Renminbi sovereign bonds.

- (2) This section applies in relation to profits tax chargeable for the year of assessment commencing on 1 April 2017 and for all subsequent years of assessment.

Clerk to the Executive Council

COUNCIL CHAMBER

2017

Explanatory Note

This Order exempts a person from the payment of profits tax chargeable under Part 4 of the Inland Revenue Ordinance (Cap. 112) in respect of sums received by, or accrued to, the person as interest or profits arising from non-Renminbi sovereign bonds.