立法會
Legislative Council

LC Paper No. CB(1)674/20-21
(These minutes have been seen by the Administration)

Ref : CB1/PL/FA

Panel on Financial Affairs

Minutes of meeting held on
Monday, 4 January 2021, at 9:30 am
in Conference Room 1 of the Legislative Council Complex

Members present	**:**	Hon Jeffrey LAM Kin-fung, GBS, JP (Chairman) Hon WONG Ting-kwong, GBS, JP (Deputy Chairman) Hon Abraham SHEK Lai-him, GBS, JP Hon Starry LEE Wai-king, SBS, JP Hon CHAN Kin-por, GBS, JP Hon Mrs Regina IP LAU Suk-yee, GBS, JP Hon MA Fung-kwok, GBS, JP Hon Christopher CHEUNG Wah-fung, SBS, JP Ir Dr Hon LO Wai-kwok, SBS, MH, JP Dr Hon Junius HO Kwan-yiu, JP Hon Holden CHOW Ho-ding Hon SHIU Ka-fai, JP Hon CHAN Chun-ying, JP Hon LUK Chung-hung, JP Hon Kenneth LAU Ip-keung, BBS, MH, JP Dr Hon CHENG Chung-tai
Member absent	**:**	Hon CHEUNG Kwok-kwan, JP
Public officers attending	**:**	<u>Agenda Item IV</u> Mr Christopher HUI, JP Secretary for Financial Services and the Treasury

Ms Salina YAN, JP
Permanent Secretary for Financial Services and the Treasury (Financial Services)

Mr Aaron LIU, JP
Deputy Secretary for Financial Services and the Treasury (Financial Services)2

Agenda Item V

Mr Christopher HUI, JP
Secretary for Financial Services and the Treasury

Ms Salina YAN, JP
Permanent Secretary for Financial Services and the Treasury (Financial Services)

Ms May CHAN, JP
Deputy Secretary for Financial Services and the Treasury (Financial Services)1

Ms Candy LAU
Principal Assistant Secretary for Financial Services and the Treasury (Financial Services)3

Ms Wings LEUNG
Deputy Commissioner (Technical) (Acting)
Inland Revenue Department

Ms Rosina LAU
Senior Assessor (Research)1
Inland Revenue Department

Mr Darryl CHAN, JP
Executive Director (External)
Hong Kong Monetary Authority

Mr Kenneth HUI
Head (Market Development)
Hong Kong Monetary Authority

Agenda Item VI

Mr Maurice LOO, JP
Deputy Secretary for Financial Services and the Treasury (Treasury)2

Miss Helen CHUNG
Principal Assistant Secretary for Financial Services and the Treasury (Treasury)(R1)

Mr LEUNG Kin-wa
Deputy Commissioner (Operations) (Acting)
Inland Revenue Department

Ms WONG Pui-ki
Chief Assessor (Profits Tax)C (Acting)
Inland Revenue Department

Ms CHAN Ut-chan
Senior Assessor (Research)3
Inland Revenue Department

Agenda Item VII

Mr Joseph CHAN, JP
Under Secretary for Financial Services and the Treasury

Mr WU Chia-chun, Desmond
Principal Assistant Secretary for Financial Services and the Treasury (Financial Services) 6

Mr LEE Chun-tung, Ricky
Assistant Secretary for Financial Services and the Treasury (Financial Services) (6) SD

Attendance by invitation : Agenda Item IV

Mr Yan-chee CHENG
Chief Corporate Affairs Officer and Executive Director
Mandatory Provident Fund Schemes Authority

Ms Gabriella YEE
Executive Director (Policy)
Mandatory Provident Fund Schemes Authority

Mr Nick SEX
Senior Director, eMPF Platform Provisional Office
Mandatory Provident Fund Schemes Authority

Clerk in attendance: Ms Connie SZETO
Chief Council Secretary (1)4

Staff in attendance : Miss Sharon LO
Senior Council Secretary (1)9

Ms Sharon CHAN
Legislative Assistant (1)4

Action

I Confirmation of minutes of meeting and matters arising

(LC Paper No. CB(1)427/20-21 — Minutes of the meeting on 2 November 2020)

The minutes of the meeting held on 2 November 2020 were confirmed.

II Information papers issued since the meeting on 7 December 2020

2. Members noted that no information paper had been issued since the meeting held on 7 December 2020.

III Date of next meeting and items for discussion

(LC Paper No. CB(1)417/20-21(01) — List of outstanding items for discussion

LC Paper No. CB(1)417/20-21(02) — List of follow-up actions)

Action

3. Members agreed to discuss the following items proposed by the Administration at the regular meeting scheduled for 1 February 2021, at 9:30am:

(a) Briefing on the work of Hong Kong Monetary Authority ("HKMA");

(b) Budget of the Securities and Futures Commission for the financial year 2021-2022; and

(c) Re-domiciliation mechanism for foreign funds.

IV Detailed proposals for taking forward the eMPF Platform project and related matters

(LC Paper No. CB(1)417/20-21(03) — Administration's paper on "Detailed proposals for taking forward the eMPF Platform project and related matters"

LC Paper No. CB(1)439/20-21(01) — Administration's letter on early withdrawal of MPF accrued benefits

LC Paper No. CB(1)417/20-21(04) — Updated background brief on the centralized electronic platform for the administration of Mandatory Provident Fund registered schemes prepared by the Legislative Council Secretariat)

Briefing by the Administration

4. At the invitation of the Chairman, Secretary for Financial Services and the Treasury ("SFST") briefed members on the legislative proposals and additional funding requirements for taking forward the eMPF Platform Project ("the Project"). He said that the eMPF Platform would be a large-scale financial infrastructure to assist Mandatory Provident Fund ("MPF") trustees in their discharge of scheme administration functions through standardization, streamlining and automation of the MPF scheme administration processes, thereby improving operational efficiency and creating room for fee reduction.

Action

Further to the completion of the first-stage legislative exercise in July 2020, the second-stage legislative amendments aimed at providing the legal basis for the designation of the eMPF Platform as the common gateway for scheme administration processes in the MPF System; delineating the respective roles, functions, powers and responsibilities of the Government, the Mandatory Provident Fund Schemes Authority ("MPFA"), the eMPF Platform Company ("the Company") (i.e. a wholly owned subsidiary to be set up by MPFA for operating the eMPF Platform) and trustees; and providing "straight pass-on" and "corresponding reduction" requirements for cost saving by trustees. The amendments would also reflect the streamlined MPF scheme administration work flow and reduced regulatory burden on trustees as a result of the implementation of the eMPF Platform. The Government planned to introduce the second-stage legislative amendments in the second quarter of 2021 with a view to securing approval of the Legislative Council ("LegCo") in July 2021, and to complete the development of the eMPF Platform by the end of 2022 at the earliest. Regarding funding requirements, SFST said that an additional funding of $1,035.646 million would be required to assist trustees in data cleansing and migration exercise, to support the use of the Government Cloud infrastructure, and to provide uncovered seed money, funding reserve and cash buffer for the Company.

Discussion

Additional fundings

5. Ir Dr LO Wai-kwok said that Members belonging to the Business and Professionals Alliance for Hong Kong supported the Project as the eMPF Platform would standardize, streamline and automate the MPF scheme administration processes, thereby improve operational efficiency and reduce scheme administration costs. He sought details on the recurrent and non-recurrent expenditure required for taking forward the Project and operating the eMPF Platform in the long run, in particular whether the provisions of $100 million for procuring insurance (in paragraph 25(b) of the Administration's paper) was a recurrent or non-recurrent expenditure item.

6. Mr CHAN Chun-ying said that he supported the proposal. He noted that according MPFA's original estimate, the cumulative quantifiable future financial savings that could be derived from the implementation of the eMPF Platform would be in the region of $22.5 billion to $23.6 billion spread over 20 years. According to the Administration's recent update, the latest guestimate was that the total cumulative quantifiable cost savings to scheme members would possibly be in a range of $30 billion to $40 billion in ten years of the operation. He enquired if the same set of assumptions were adopted in working out the latest guestimate. He also sought clarification on whether the seed money and insurance costs

(paragraph 25(b) of the Administration's paper) were recurrent or non-recurrent in nature, and whether the proposed cash buffer of $378 million for the Company (paragraph 25(c) of the Administration's paper) could be provided in phases and whether the Government could recover the cost when the Company had surplus.

7. Permanent Secretary for Financial Services and the Treasury (Financial Services) ("PS(FS)") advised that some $3,900 million of non-recurrent funding provisions had been approved by LegCo for the Project covering the costs on development of the information technology ("IT") infrastructure and software applications, and the operating costs of the Company in its first two years of set-up. The operating costs of the eMPF Platform thereafter would be recovered from fees payable by trustees for using the Platform, and the estimated operating expenditure of the Company was about $130 million per annum on average. In respect of the proposed additional non-recurrent funding for the Project, they were to assist trustees in their data cleansing and migration, to support the use of Government Cloud, and to provide uncovered seed money, funding reserve and cash buffer for the Company. As regards the proposed $100 million provision for the Company mentioned in paragraph 25(b) of the paper, it was an estimated expenditure to cover the potential liabilities of the Company in performing its duties and functions. Regarding the cash buffer, PS(FS) said that the funding was required for meeting the unforeseeable cash-flow needs of the Company due to fluctuation of the market situation and the fee income. To monitor the use of the capital grant and expenditures of the Company, a tripartite grant agreement would be signed between the Government, MPFA and the Company. The proposed cash buffer would be disbursed to the Company only if necessary having regard to the projected cash flow requirements and financial position of the Company, which would be reviewed under the annual budgeting cycle. Given the Company's governance structure and financial reporting arrangement, the use of cash buffer if granted would be transparent and subject to close monitoring by the Company's Board and the Government.

Possible cost savings

8. Mr LUK Chung-hung was of the view that the industry-wide fund expenses ratio of around 1.44% out of the asset under management ("AUM") was relatively high considering the low investment return of MPF funds. While it was estimated that the eMPF Platform fee to be charged by the Company would be in a range of 0.3% to 0.4% of AUM in the transitional stage, and would further drop to 0.2% to 0.25% in about ten years' time, Mr LUK enquired how the Administration would ensure scheme members could benefit from the cost savings, and whether the Administration would consider setting a cap on fees of MPF funds so as to ensure trustees, after reducing the fees under the "straight pass-on" requirement, would not raise the fees again in the future. He further

asked if the Administration would consider further lowering the fee cap for the two constituent funds under the Default Investment Strategy, and the timetable for the implementation of full portability of MPF benefits which would help promote market competition and in turn help drive down fees and charges further.

9. Ir Dr LO Wai-kwok urged the Administration to ensure that scheme members could benefit from possible savings in scheme administration costs after the implementation of the eMPF Platform, and trustees would not charge fees on other pretexts.

10. SFST said that currently, MPF schemes were operated by 14 trustees under a decentralized landscape involving 12 scheme administration platforms with different standards. The multiple business models, data standards, process designs and administration system infrastructure of the MPF System had contributed to the high administration costs of the System. The policy objective of the Project was to achieve cost savings from the enhanced operational efficiency of the MPF System, thereby creating room for fee reduction for the benefit of scheme members. To achieve the policy objective and ensure that any cost savings derived from the Platform operation would be passed directly to scheme members, two statutory requirements were proposed. First, there should be a statutory requirement that no fee on scheme administration exceeding the eMPF Platform fee payable by trustees to the Company could be charged, whether in whole or in part, to the scheme, a constituent fund of the scheme, or a member of the scheme (i.e. the "straight pass-on" requirement). Second, with the lowered scheme administration costs due to the eMPF Platform, there should be corresponding reduction in the topline fees of MPF schemes. He added that the eMPF Platform fee to be charged by the Company in the transitional stage would be in a range of 0.3% to 0.4% of AUM. This represented the first stage of fee reduction to scheme members upfront by a possible 30% cut in scheme administration costs on average. Depending on the rate of digital take-up and consequential improvement to operational efficiency, it was expected that the eMPF Platform fee would further drop in a gradual and steady manner to 0.2% to 0.25% in about ten years' time.

11. Mr Holden CHOW enquired if the Administration would consider, as a long-term strategy, requiring trustees to charge scheme members a fixed amount of scheme administration fees instead of basing on a percentage of AUM.

12. Mr WONG Ting-kwong expressed concern that the magnitude of cost savings might not be fully realized in the early stage of transition given that trustees needed to incur additional costs and make investment in system adjustment for interfacing and inter-operability, data cleansing and migration as well as risk management for moving to the eMPF Platform. He commented that

the Administration should provide a timetable for realizing fee reduction ensuring scheme members could benefit from the cost savings soonest possible, and urged the Administration to strengthen cost control of the Project.

13. The Chairman urged the Administration to continue engaging MPF trustees with a view to ensuring that trustees would lower their scheme administration fees as early as possible after the implementation of the eMPF Platform.

14. SFST reiterated that the objective of the eMPF Platform was to enhance the efficiency of the MPF System, thereby providing more room for fee reduction to benefit scheme members through switching from the predominantly paper-based MPF-related transactions at present to primarily electronic means in future under the eMPF Platform. In formulating the proposals on eMPF Platform fee, one of the most important guiding principles was to maximize the room for fee reduction for the benefit of scheme members. Assuming a high level of digital take-up rate and with economies of scale, it was estimated that the total cumulative quantifiable cost savings to scheme members would possibly be in a range of $30 billion to $40 billion over a ten-year period. Moreover, it was expected that after the trustees got onboard the eMPF Platform during the two-year transitional stage, scheme members could enjoy upfront a fee cut of around 30% on average in scheme administration (i.e. from 0.58% to about 0.3% to 0.4%). He further said that any change in the MPF fee-charging mechanism would be a fundamental policy change. Before proposing any substantive changes to the current mechanism, factors like the impact on the operation of the MPF System and benefits to scheme members must be carefully considered and assessed.

Views and concerns of MPF trustees

15. Mr CHAN Chun-ying referred to the submission from 14 MPF trustees expressing views and concerns on the Project, particularly the latest guestimate on possible cost savings that could be derived from the implementation of the eMPF Platform, the prevailing scheme administration fees charged by the trustees, immunity and liability of the Platform, etc., and urged the Administration and MPFA to further discuss with the MPF industry and reach a consensus before seeking funding approval from LegCo.

16. Mr Christopher CHEUNG expressed support for the implementation of eMPF Platform. As MPF trustees would incur costs in upgrading their IT systems for getting onboard to the eMPF Platform, he enquired if the Administration would consider providing financial assistance to trustees for this purpose, and what measures the Administration and MPFA would take to encourage trustees to

support the full operation of the eMPF Platform. Moreover, he noted that some MPF trustees considered the Government's estimate on the possible cost savings of $30 billion to $40 billion to scheme members in ten years of the operation over optimistic, and enquired how the future eMPF Platform fee would be determined.

17. Mr CHAN Kin-por said that the MPF industry was supportive of the Project and willing to work with the Government and MPFA to ensure a smooth, fair, reasonable and transparent transition from the existing system to the new eMPF Platform. He opined that the policy objective of the Project (i.e. lowering the fees of MPF System) could be achieved by simplifying the administrative functions and streamlining the processes of the MPF System, thereby enhancing efficiency and driving down costs, including regulatory burden and compliance costs of trustees. He referred to the submission from 14 MPF trustees and highlighted the main concerns of the industry including (a) the scheme administration functions that would be performed by the eMPF Platform; (b) the 0.58% scheme administration costs adopted for estimating the possible cost savings of $30 billion to $40 billion in ten years of the operation; and (c) safeguards to trustees if non-compliance with the statutory requirements was due to the partial (instead of sole) failure of the eMPF Platform/Company. He added that to allow the Government and MPFA to have a better estimate on the possible cost savings arising from the operation of the eMPF Platform, the trustee industry had proactively provided information on the scheme administration fees currently charged by trustees. The industry considered that the possible cost savings of $30 billion to $40 billion in ten years of the operation as estimated by MPFA, which had been calculated based on the 0.58% scheme administration costs, might be overstated. Moreover, he strongly requested the Government and MPFA to meet with the MPF industry to discuss and clarify the issues raised by the trustees with a view to addressing their concerns and reaching a consensus before submitting the funding proposal to LegCo.

18. SFST recognized that the concerted effort of the Government, MPFA and MPF trustees was pivotal to the successful implementation and smooth operation of the eMPF Platform. To this end, the Government and MPFA had set up the Working Group on eMPF in 2017 to steer the development of the Platform in collaboration with the MPF trustees. Amongst other things, the Working Group had formulated a set of common standards and technical specifications covering most areas of MPF scheme administration processes, which formed the scope of the tender documents of the eMPF Platform. The Government noted that trustees would incur expenditure for data cleansing and migration in order to transfer to the eMPF Platform. Hence, an additional funding provision of $210 million was proposed to facilitate trustees' boarding onto the eMPF Platform and managing the associated risks. He added that details of the assistance to be provided to trustees, particularly the first batch for boarding onto the eMPF Platform, would

be worked out between MPFA, the Company and trustees during discussions on the transitional arrangements. He stressed that the implementation of the eMPF Platform would not change the existing relationship between MPFA as a regulator and the trustees as regulatees. Therefore, trustees should continue to owe fiduciary duties to scheme members and would remain legally responsible for the administration of MPF schemes after the implementation of the eMPF Platform. For other services currently provided by trustees which were not directly relevant to their obligations under MPF legislation (e.g. customer service hotline), or were more personalized or "add-on" services to tailor to different customers' experience or needs, the eMPF Platform would not take up these functions as they were not core scheme administration functions and trustees or their group companies might continue to provide as part of their business running costs. He assured members that the Government and MPFA would continue to have on-going dialogue with the MPF industry to ensure smooth and secure transition from the existing system to the new eMPF Platform.

19. In response to Mr Christopher CHEUNG's enquiry about the timetable for implementation of the eMPF Platform, SFST advised that the hardware and software development of the Platform was expected to complete by the end of 2022 at the earliest. Subject to orderly transition by trustees in batches starting from 2023, the eMPF Platform would come into full operation in around 2025.

Early withdrawal of accrued benefits of MPF schemes

20. Dr CHENG Chung-tai pointed out that the Administration's refusal to allow members of the public to make early withdrawal of MPF accrued benefits in the current difficult period of time had indicated its failure in understanding public opinion and sentiment. He urged that the Administration should consider relaxing the withdrawal conditions by allowing members of the public who were in financial distress to partially withdraw their MPF accrued benefits for meeting their immediate needs. He also expressed concern that scheme members might need to fulfil more stringent requirements if they withdraw MPF accrued benefits on the grounds of permanent departure from Hong Kong after the implementation of the eMPF Platform. For example, supporting documents for withdrawal like the Home Visit Permit, which at present were acceptable by trustees as evidence proving that the scheme member was permitted to reside in a place other than Hong Kong, might not be accepted by the eMPF Platform.

21. Mr Holden CHOW expressed disappointment that the Administration had refused the suggestion of allowing members of the public to partially withdraw their MPF accrued benefits for meeting their financial hardship.

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22. The Chairman sought elaboration on the conditions for early withdrawal of MPF accrued benefits by scheme members on the grounds of permanent departure from Hong Kong.

23. SFST stressed that the MPF System was designed as a long-term saving scheme for retirement. Any proposals allowing early withdrawal of accrued benefits from MPF System must take into consideration the corresponding reduction of scheme members' accrued benefits meant for their retirement. If the preservation requirement on accrued benefits was relaxed and scheme members were allowed to make early withdrawal to meet short-term financial needs or contingency, the accrued benefits would be leaked from the System from time to time and the function of accumulation for value growth would be weakened, thereby undermining the integrity of the MPF System and rendering it difficult to achieve the purpose of assisting the working population to save for their retirement. Hence, after detailed deliberation within the Government and thorough consideration of relevant policy objectives and long-term implications, it was considered not appropriate to allow early withdrawal of MPF accrued benefits by scheme members for addressing their imminent needs. Regarding the conditions for early withdrawal of MPF accrued benefits, SFST said that the MPF legislation had clearly stipulated the circumstances and requirements for such withdrawal, including on the grounds of permanent departure from Hong Kong.

Conclusion

24. The Chairman concluded that Panel members had no objection to the Administration's plan of seeking approval for additional funding for the Project, and introducing the second-stage legislative amendments into LegCo in the second quarter of 2021.

V Tax concession for carried interest

(LC Paper No. CB(1)417/20-21(05) — Administration's paper on "Tax concession for carried interest")

Briefing by the Administration

25. At the invitation of the Chairman, SFST briefed members on the Administration's legislative proposals to: (a) provide tax concessions for carried interest distributed by eligible private equity ("PE") funds operating in Hong Kong; and (b) enhance the profits tax regime for privately offered funds by expanding the scope of financial assets that could be held and administered by the

special purpose entities established by funds. The proposed tax concessions would apply to eligible carried interest arising from the qualifying transactions of an investment fund certified by HKMA ("certified investment fund") or a return paid by The Innovation and Technology Venture Fund Corporation ("the ITVF Corporation") to its co-investment partners. A qualifying carried interest recipient had to provide investment management services in Hong Kong to a certified investment fund or the ITVF Corporation and meet the substantial activities requirements ("SARs"). Under the proposed tax concession regime for carried interest ("tax concession regime"), in respect of qualifying carried interest recipients, eligible carried interest would be charged at profits tax rate of 0%. Besides, 100% of eligible carried interest would be excluded from the employment income for the calculation of salaries tax. The concessionary tax treatment would apply to eligible carried interest received by or accrued to qualifying carried interest recipients on or after 1 April 2020. The Administration planned to introduce the amendment bill ("the Bill") into LegCo in early February 2021.

Discussion

Development of the private equity fund industry in Hong Kong

26. Mr CHAN Chun-ying expressed support for the tax concession regime in general. He enquired whether the task force led by the Financial Services and the Treasury Bureau ("Task Force") had studied other measures to develop Hong Kong as a premier PE fund hub and whether it had made reference to other jurisdictions such as the Mainland and Singapore in developing the regime. Mr CHAN also enquired about the rationale for proposing the concessionary tax treatment to take retrospective effect to apply to eligible carried interest received by or accrued to qualifying carried interest recipients on or after 1 April 2020.

27. SFST advised that the Task Force would continue to review various measures to promote the development of PE fund industry in Hong Kong. For instance, the Administration was formulating legislative proposals to allow foreign funds to re-domicile to Hong Kong as Limited Partnership Funds ("LPFs") or Open-ended Fund Companies. As the growth of Hong Kong's PE fund industry was relatively slower than competitors including Singapore, it was necessary for Hong Kong to step up effort in enhancing its competitive edge on this front. Concerning the retrospective effect, SFST explained that the proposed tax concession regime was announced in the 2020-2021 Budget Speech. The Administration had to take swift action in expediting the development of PE fund industry in Hong Kong.

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28. Executive Director (External), Hong Kong Monetary Authority ("ED(E)/HKMA") added that HKMA had been engaging the PE fund industry on possible enhancements to attract PE funds to Hong Kong. The industry in general considered various factors when choosing the location to set up and operate a fund. These included investment opportunities, location of investors, supply of talents as well as professional services support, where Hong Kong had been all along very competitive. There were however two areas of concern, i.e. the lack of a modern legal framework for the establishment of LPFs and a competitive tax regime for carried interest distributed by PE funds. The Administration had introduced the Limited Partnership Fund Bill in 2020 (which was enacted as the Limited Partnership Fund Ordinance (Cap. 637) in August 2020) to enable the establishment of an investment fund in Hong Kong in the form of a limited partnership. The proposed tax concession regime was another measure to attract PE funds to operate in Hong Kong.

29. Ir Dr LO Wai-kwok expressed support for the legislative proposals in principle. He pointed out that the present proposals were more related to supply side measures with the aim to attract PE funds to operate in Hong Kong, and enquired whether the Administration had studied the demand for PE funds in the Hong Kong capital chain, and developed measures to promote the development of PE fund sector in Hong Kong.

30. SFST advised that the demand side of Hong Kong's capital chain included demand for investment opportunities and demand for financing opportunities. In respect of increasing the demand of investment opportunities, the Administration would introduce measures including promoting the development of family office business in order to increase the demand for PE investments. On the other hand, the Administration would develop Hong Kong as an innovation hub and promote the development of financial technologies so that companies in the relevant sectors would create financing opportunities for PE funds.

Benefits of the proposed tax concession regime for carried interest

31. Dr Junius HO enquired if the Administration had assessed the quantifiable benefits including the new investment opportunities to be brought by the proposed tax concession regime, and estimated the revenue forgone arising from the regime. He also enquired whether the Administration had estimated or set any target on the amount of capital under management by PE funds in Hong Kong after the implementation of the regime.

32. Mr LUK Chung-hung had reservation over providing tax concessions for carried interest of PE funds as a measure to attract more PE funds to operate in Hong Kong. He opined that the development of PE fund industry also relied on

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the availability of talents. As most members of the public were unable to invest in PE funds owing to their extremely high investment thresholds, he was concerned that there would be criticisms that the proposed tax concession regime was leaned towards the wealthy people and PE fund industry. Mr LUK considered that the Administration and HKMA should provide information on: (a) the estimated revenue forgone arising from the proposed tax concession regime; and (b) how the proposed regime could benefit Hong Kong, including quantitative benefits on new investment opportunities and the estimated number of jobs to be created.

33. The Chairman said that the business sector welcomed that the Administration had adopted some suggestions made by the industry in formulating the legislative proposals, and agreed that Hong Kong should make reference to measures of other jurisdictions in attracting PE funds. He considered that the benefits brought by the development of PE fund industry in Hong Kong could offset the revenue forgone arising from the proposed tax concession regime, and enquired about the Administration's assessment on how the proposed tax concession regime would promote Hong Kong's economic development and enhance its status as an international financial centre.

34. SFST said that it would be difficult to quantify the benefits of the proposed tax concession regime on Hong Kong. He reiterated that Hong Kong had already lagged behind its competitors including Singapore in the development of PE fund industry. The situation could aggravate as Hong Kong's competitors were offering competitive tax rates on carried interest distributed by PE funds. So there was a pressing need to introduce the proposed tax concession regime to sharpen Hong Kong's competitive edge on this front. SFST added that there were some 560 PE firms in Hong Kong in 2019. It was envisaged that the number would likely increase upon implementation of the proposed tax concession regime. Moreover, the development of PE fund industry could in turn enhance the ecosystem and value chain of Hong Kong's financial services sector. SFST agreed to provide information as requested by Mr LUK Chung-hung. As for whether the proposed tax concession regime was leaned towards the PE fund industry, SFST explained that unlike management fees, the earning of carried interest involved high investment risks. He also stressed that SARs and anti-avoidance provisions set out in the legislative proposals could prevent abuse of the proposed tax concessions.

35. ED(E)/HKMA said that the amount of capital under management by PE funds in Hong Kong was around US$ 170 billion in the third quarter of 2020. He added that the complexities involved in the assessment of carried interest of PE funds made it difficult to work out the estimated amount of revenue forgone arising from the proposed tax concession regime. Such complexities included the industry practice for a PE fund to hold its investment for a few years, and that

carried interest would only arise if there were profits when the investment was disposed of with such profits meeting certain hurdle rate. It was believed that local employment would be boosted if more PE funds were attracted to Hong Kong. Besides, additional management fees paid to fund managers would be taxed in Hong Kong, generating additional tax revenue.

(*Post-meeting note:* The supplementary information provided by the Administration and HKMA was circulated to members vide LC Paper No. CB(1)538/20-21(02) on 27 January 2021.)

36. Mr Holden CHOW said that he supported the direction of the legislative proposals. He asked how the Administration would make use of the spill-over effects of PE funds to promote the development of other industries in Hong Kong. He further suggested that the Administration should consider designating a site in Hong Kong to facilitate the development of a PE fund cluster, which would in turn help boost other related industries and enhance local employment.

37. SFST responded that PE funds had many spill-over effects like strengthening Hong Kong's role as an international financial and innovation centre. It was envisaged that the development of PE fund industry would not only enhance Hong Kong's financial ecosystem but also increase the demand for various professional services including legal and accounting services. ED(E)/HKMA added that a study conducted by the Financial Services Development Council had estimated that one PE fund job could create up to three to six new jobs in related services industries, such as accounting, legal and financial services.

Implementation details of the proposed tax concession regime for carried interest

38. Mr CHAN Chun-ying noted that one of the SARs under the proposed tax concession regime was that the operating expenditure incurred by a qualifying carried interest recipient in Hong Kong for the provision of investment management services to a certified investment fund or the ITVF Corporation for each year of assessment should be Hong Kong dollar ("HK$") two million or more. As some overseas companies registered in Hong Kong generated most of their profits from businesses in other jurisdictions, he asked how the Administration would enforce the above requirement and whether there would be practical criteria for measuring companies' compliance with the requirement. Mr CHAN also enquired whether the Administration had assessed the impact of the proposed tax concession regime on the proportion of resident and non-resident funds in Hong Kong.

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39. Mr Holden CHOW said that some PE funds might allocate their capital in various jurisdictions, and enquired whether there would be requirement for PE funds to allocate most of their capital in Hong Kong in order to be eligible for the proposed tax concession regime.

40. SFST and ED(E)/HKMA responded that the Administration would not restrict the allocation of capital as free capital flow was one of Hong Kong's existing strengths and an important feature of an international financial centre. Besides, PE funds in general would not concentrate their capital in a single jurisdiction as they looked for suitable investment opportunities around the world. The Administration would thus focus on attracting PE funds to conduct business activities in Hong Kong and the Guangdong-Hong Kong-Macao Greater Bay Area.

41. While expressing support for the legislative proposals, Mr Christopher CHEUNG suggested that the proposed tax concession regime should be extended to cover local securities firms licensed to carry out Type 9 regulated activities (i.e. asset management) so that a level playing field would be provided between the local brokerage firms and the PE fund sector. In his view, the extension would benefit Hong Kong's economic development and the employment market.

42. SFST explained that the proposed tax concession regime was confined to PE funds as the business nature of PE funds was different from that of local securities firms. For instance, PE funds faced greater risks as they usually invested in budding private companies and start-ups.

Conclusion

43. The Chairman concluded that Panel members had no objection to the Administration's plan of introducing the Bill into LegCo in early February 2021.

VI Inland Revenue (Amendment) (Qualifying Amalgamations, Specified Assets and Furnishing of Returns) Bill 2021

(LC Paper No. CB(1)417/20-21(06) — Administration's paper on Inland Revenue (Amendment) (Qualifying Amalgamations, Specified Assets and Furnishing of Returns) Bill 2021)

Action

Briefing by the Administration

44. At the invitation of the Chairman, Deputy Secretary for Financial Services and the Treasury (Treasury)2 ("DS(Tsy)2") and Deputy Commissioner (Operations) (Acting), Inland Revenue Department briefed members with the aid of a powerpoint presentation on the Administration's proposal to amend the Inland Revenue Ordinance (Cap. 112) ("IRO") to address matters relating to: (a) the tax treatment for amalgamation of companies under the court-free procedures as provided for under the Companies Ordinance (Cap. 622); (b) the tax treatment for transfer or succession of specified assets under certain circumstances; and (c) the filing of tax returns by electronic means ("e-filing"). The Administration planned to introduce the relevant amendment bill ("the IRO Bill") into LegCo in March or April 2021.

(*Post-meeting note*: The powerpoint presentation materials (LC Paper No. CB(1)441/20-21(01)) were issued to Members vide Lotus Notes e-mail on 4 January 2021.)

Discussion

Implementation details of the legislative proposals

45. Mr CHAN Chun-ying requested the Administration to elaborate the benefits of the IRO Bill, including the types of economic activities the Administration planned to promote through the Bill. He asked whether the Administration would adopt his suggestion of providing the group loss relief treatment under the IRO Bill to cover certain activities (such as research and development activities and construction of environmental protection facilities) carried out by companies not undergoing amalgamation.

46. The Chairman expressed support for the present proposal but was disappointed that the Administration had not taken into account business sector's views in formulating the proposal. He stressed the need for the Administration to make reference to other jurisdictions' practices in providing favourable tax treatment to companies in those jurisdictions when introducing special tax treatment to companies in Hong Kong. He also opined that the Administration should provide concrete justifications for the present proposals.

47. DS(Tsy)2 said that the legislatives proposals on the tax treatment for court-free amalgamation of companies and transfer or succession of specified assets without sale were technical amendments to IRO, and it would be difficult to quantify their economic benefits. Nevertheless, such amendments would provide certainty for companies on the tax treatment concerned, and hence would

facilitate the conduct of businesses. Moreover, the legislative proposals on e-filing could lower the compliance costs of companies. On the issue of group loss relief tax treatment, DS(Tsy)2 advised that the Administration had to examine the matter carefully as it would have far reaching implications on the Government's profits tax revenue. He also pointed out that the Organisation for Economic Co-operation and Development was currently drawing up proposals for imposing a global minimum tax on large multinational companies under the Base Erosion and Profit Shifting 2.0 package, and such proposals would offset the tax benefits of group loss relief should it be offered to such companies.

48. Mr Christopher CHEUNG expressed support for the legislative proposals. Noting that the special tax treatment to be applicable to court-free qualifying amalgamations covered the set-off of unutilized pre-amalgamation losses of the amalgamating company against the assessable profits of the amalgamated company (i.e. paragraph 6(d) of the Administration's paper), Mr CHEUNG was concerned that the tax treatment could be abused by companies through shell companies, and enquired how the Administration would tackle the problem.

49. DS(Tsy)2 responded that the application of the tax treatment concerned would be subject to a number of restrictions and conditions including the same trade test (i.e. qualifying losses could only be used to set off against the assessable profits of the amalgamated company derived from the same trade, profession or business it succeeded from the amalgamating company). Companies failing to meet such restrictions and conditions would not be able to enjoy the tax treatment concerned. There would also be anti-avoidance provisions to prevent abuse.

Filing of tax returns by electronic means

50. Mr CHAN Chun-ying enquired about the scale of the 2 200 companies which had submitted tax returns through the existing eTax Portal during the year ended 31 March 2020, and measures taken or planned by the Administration for encouraging companies to use the eTax Portal. The Chairman said that while the Administration advocated the use of e-filing, it should address existing problems of the eTax Portal (e.g. the inability of the Portal to accept financial statements).

51. DS(Tsy)2 responded that at present most companies using the existing eTax Portal were small companies. Relatively few large companies used the eTax Portal as the system currently could not accept the financial documents submitted by such companies due to its limited uploading capacity. The Finance Committee had approved a new commitment of about $742 million for the enhancement and relocation of IT systems and facilities of the Inland Revenue Department for the new Inland Revenue Tower in the Kai Tak Development Area, including the development of a new Business Tax Portal. It was envisaged that more large

companies would submit tax returns by electronic means when the new Business Tax Portal, which would enable the Department to receive voluminous accounting and financial data electronically, was scheduled to be launched in around 2023.

Conclusion

52. The Chairman concluded that Panel members had no objection to the Administration's plan of introducing the IRO Bill into LegCo in March or April 2021.

(At 11:55am, the Chairman ordered that the meeting be extended for 15 minutes to 12:15 pm to allow sufficient time for discussion.)

VII Contribution of Hong Kong to the 12th replenishment of the Asian Development Fund

(LC Paper No. CB(1)417/20-21(07)	—	Administration's paper on "Asian Development Bank - Contribution of Hong Kong to the 12th replenishment of the Asian Development Fund"
LC Paper No. CB(1)417/20-21(08)	—	Background Brief on Hong Kong's contribution to the 12th replenishment of the Asian Development Fund prepared by the Legislative Council Secretariat)

Briefing by the Administration

53. At the invitation of the Chairman, Under Secretary for Financial Services and the Treasury ("USFST") briefed members on the proposed contribution of US$16.08 million (about HK$126.99 million) to the 12th replenishment of the Asian Development Fund (or "ADF 13") of the Asian Development Bank ("ADB"). He explained that ADF was typically replenished once every four years and contribution to ADF was voluntary. The Administration's proposal was to maintain Hong Kong's burden share at 0.57% of the target donor contributions, which was the same ratio adopted in the past six ADF replenishments since 1997. The Administration would adopt a 11-year standard encashment schedule

(i.e. from 2021-2022 to 2031-2032) for Hong Kong's contribution to ADF 13, and include the required provision in the draft Estimates of the relevant financial years.

Discussion

Hong Kong's contributions to the Asian Development Fund

54. Mr CHAN Chun-ying supported Hong Kong to continue contributing to ADF 13. He enquired about the contribution to be made by Singapore and its burden share ratio in ADF 13. Pointing out that Hong Kong would suffer from fiscal deficits in 2021, Mr CHAN enquired whether the 11-year encashment schedule could be adjusted so that Hong Kong could pay a lower rate of contribution in the first few years of the schedule.

55. USFST responded that Singapore's current shareholding in ADB and burden share ratio were both lower than those of Hong Kong. Singapore had maintained its burden share ratio in ADF 13 (which amounted to US$ 4.23 million). Many ADB members had indeed maintained or even increased their burden share ratios in ADF 13. As regards the 11-year encashment schedule, USFST pointed out that it was set by ADB after deliberation amongst Members.

Hong Kong's representation at the Asian Development Bank

56. Mr CHAN Chun-ying enquired whether Hong Kong's representation arrangement at ADB (i.e. representation by the Australian Director in the Board of Directors of ADB) would remain unchanged, and about the details of the Hong Kong officers attached to the office of the Australian Director.

57. USFST confirmed that Hong Kong's representation arrangement at ADB remained unchanged. The Administration attached a Senior Administrative Officer to the office of the Australian Director from 2017 to 2019, and planned to deploy another secondee to the office in 2025.

Participation of Hong Kong firms in projects financed by the Asian Development Bank

58. Mr Holden CHOW noted that the Mainland had increased its burden share ratio in ADF 13 and expressed support for Hong Kong maintaining its contribution to ADF 13. He asked how the Administration would help Hong Kong companies to bid ADB-financed projects, and whether the Administration had estimated the amount of contracts awarded by ADB to

Action

Hong Kong companies in 2020 and beyond. Mr CHAN Chun-ying made a similar enquiry.

59. USFST highlighted the benefits of Hong Kong's contribution to ADF as set out in the Administration's paper. He pointed out that some Hong Kong companies were awarded ADB's contracts in 2020. While the relevant amount or value of contracts in 2020 were not yet available, Hong Kong service providers had been awarded US$976.4 million cumulatively up to the end of 2019. It would be difficult to estimate the amount of contracts to be awarded by ADB to Hong Kong companies in the coming few years. However, it was observed that the amount of bonds issued by ADB in Hong Kong remained steady from 2016 to 2019 (i.e. in the range of US$ 200 million to US$ 400 million per year). The Administration would continue to work in collaboration with the Hong Kong Trade Development Council to improve the dissemination of information on ADB-financed projects and facilitate contact between local companies and staff of ADB. It would also promote Hong Kong's strength in financial services to ADB.

Promoting the work of the Asian Development Bank

60. Dr Junius HO supported the proposed contribution to ADF 13. He opined that the Administration should promote the successful experience of economic development in the Mainland and that of the Belt and Road Initiative. The Financial Services and Treasury Bureau should also liaise with the Radio Television Hong Kong and encourage the latter to report such experience in an objective manner.

61. USFST responded that the Administration would continue promoting the work of ADB and the Asian Infrastructure Investment Bank to the community as appropriate.

Conclusion

62. The Chairman concluded that members had no objection to the Administration's proposed contribution of US$16.08 million to ADF 13.

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VIII Any other business

63. There being no other business, the meeting ended at 12:15 pm.

Council Business Division 1
Legislative Council Secretariat
16 March 2021