

LEGISLATIVE COUNCIL BRIEF

**Inland Revenue Ordinance
(Chapter 112)**

REVENUE BILL 2004

PURPOSE

At the meeting of the Executive Council on 20 April 2004, the Council ADVISED and the Chief Executive ORDERED that the Revenue Bill 2004, at *Annex A*, should be introduced into the Legislative Council to implement certain revenue-related proposals announced in the 2004-05 Budget.

JUSTIFICATIONS

Extension of Home Loan Interest Deduction Entitlement Period under Salaries Tax and Personal Assessment

2. The 5-year salaries tax deduction for home loan interest was introduced in 1998/99 as a temporary measure to provide relief to taxpaying households heavily burdened with home mortgage payments. For taxpayers who have acquired their homes in the year 1998/99 or before and have since 1998/99 claimed the deduction continuously, the five-year entitlement period will have expired in the 2003/04 year of assessment.

3. Though the burden of home mortgage repayments on taxpayers in general is lighter now than when the deduction was introduced due to the fall in property prices and the drop in mortgage interest rates, as a relief to all home owners and to ease the heavy financial load still borne by many families, we propose to extend the entitlement period for home loan interest deduction for two years, that is, from any five tax years to any seven years of assessment, with the maximum deduction in any year

maintained at \$100,000. The concession will take effect from the 2003/04 year of assessment. Several hundred thousand taxpayers will benefit from this measure.

Extension of Scope of Profits Tax Deduction for Research and Development Expenses

4. The Inland Revenue Ordinance has all along provided profits tax deduction for most expenses on research and development. However, the deduction does not cover capital expenses on design-related activities. To facilitate the proposed "DesignSmart" initiative which aims to strengthen our support for design and innovation, we propose to extend the profits tax deduction for research and development expenses to cover such expenses. After the proposed extension, the scope of research and development expenditure deduction allowed under our regime will compare favourably with other jurisdictions.

OTHER OPTIONS

5. We must amend the existing legislation in order to bring the revenue proposals announced in the 2004-05 Budget into effect. There is no other option.

THE BILL

6. The purpose of this Bill is to amend the Inland Revenue Ordinance (Cap. 112) to give effect to some of the proposals in the 2004-05 Budget. The major provisions are as follows: -

- (a) **Clause 3** amends section 26E to increase the number of years for which deductions for home loan interest paid by a person are allowable, from five years of assessment to seven years of assessment; and
- (b) **Clauses 2, 4 and 5** amend sections 16B, 37A and 40 to replace references to "scientific research" with references to "research and development" and expand the scope of research and development activities, expenditure on which is deductible for

profits tax purpose.

7. The existing provisions proposed to be amended are at *Annex B*.

LEGISLATIVE TIMETABLE

8. The legislative timetable will be -

Publication in the Gazette	23 April 2004
First Reading and commencement of Second Reading debate	28 April 2004
Resumption of Second Reading debate, committee stage and Third Reading	To be notified

IMPLICATIONS OF THE PROPOSAL

9. The proposal is in conformity with the Basic Law, including the provisions concerning human rights. The proposal will not affect the binding effect of the existing provisions of the Ordinance and its subsidiary legislation. It has no productivity, environmental, civil service or sustainability implications.

Financial Implications

10. It is estimated that the proposal to extend the limit for home loan interest deduction by two years will cost the Government \$4.6 billion in tax revenue over five years. The proposal to extend the profits tax deduction for research and development expenses to cover expenses on design-related activities will cost \$30 million in a full year.

Economic Implications

11. The proposed legislative amendments are required to implement some of the revenue-related measures announced in the 2004-05 Budget. These revenue measures are part and parcel of the whole package of

budgetary measures, which taken together will allow the community and enterprises a respite in which to build up their strength, thereby being conducive to a sustained economic recovery. The individual revenue-related measures on their own are not expected to have any significant impact on the overall economy.

PUBLIC CONSULTATION

12. The Financial Secretary conducted consultations with Legislative Council Members, various chambers, groups and associations as well as the general public during the formulation of the 2004-05 Budget. The views they expressed have been taken into account.

PUBLICITY

13. We will issue a press release. A spokesman will be available to answer media and public enquiries.

BACKGROUND

14. In the 2004-05 Budget, the Financial Secretary made, among others, the following revenue-related proposals -

- (a) to extend the entitlement for home loan interest deduction under salaries tax and personal assessment from five to seven years of assessment with effect from the 2003/04 year of assessment; and
- (b) to extend the scope of deduction for research and development expenses under profits tax to cover design-related expenses with effect from the 2004/05 year of assessment.

15. We have to amend the Inland Revenue Ordinance to implement these proposals.

ENQUIRY

16. In case of enquiries about this Brief, please contact Miss Erica NG, Principal Assistant Secretary for Financial Services and the Treasury (Treasury)(Revenue), at 2810 2370.

Financial Services and the Treasury Bureau
20 April 2004

A BILL

To

Amend the Inland Revenue Ordinance to give effect to some of the proposals in the Budget introduced by the Government for the 2004-2005 financial year.

Enacted by the Legislative Council.

1. Short title, application and commencement

(1) This Ordinance may be cited as the Revenue Ordinance 2004.

(2) This Ordinance, except section 3, shall apply in relation to the year of assessment commencing on 1 April 2004 and to all subsequent years of assessment.

(3) Section 3 shall be deemed to have come into operation on 1 April 2003.

Inland Revenue Ordinance

2. Expenditure on research and development

Section 16B of the Inland Revenue Ordinance (Cap. 112) is amended -

- (a) in subsection (1)(a) and (b), by repealing "scientific research" wherever it appears and substituting "research and development";
- (b) in subsection (3) -
 - (i) in paragraph (a), by repealing "scientific research" where it twice appears and substituting "research and

development";

(ii) by adding -

"(d) Where, prior to the commencement of section 2 of the Revenue Ordinance 2004 (of 2004), expenditure represented by any plant or machinery has been allowed as a deduction in ascertaining the profits from a trade, profession or business pursuant to the provisions of subsection (1)(b) in force immediately before that commencement, then, for the purposes of paragraph (a) -

(i) such plant or machinery shall be treated as plant or machinery representing research and development expenditure of a capital nature which had been allowed as a deduction in ascertaining the profits from the trade, profession or business pursuant to

subsection (1)(b);

and

(ii) the reference in that paragraph to the amount of the deduction in respect of expenditure represented by such plant or machinery shall be construed as a reference to the aggregate of -

(A) the amount of the deduction allowed in respect of expenditure represented by such plant or machinery pursuant to the provisions of subsection (1)(b) in force immediately before that commencement; and

(B) the amount of the deduction allowed in respect of research and

development
expenditure of a
capital nature
represented by
such plant or
machinery
pursuant to
subsection (1)(b)
after that
commencement.";

(c) in subsection (3A) -

(i) in paragraph (a), by repealing
"scientific research" where it twice
appears and substituting "research and
development";

(ii) by adding -

"(c) Where, prior to the
commencement of section 2 of
the Revenue Ordinance 2004
(of 2004), expenditure to
which any rights relate has
been allowed as a deduction in
ascertaining the profits from a
trade, profession or business
under the provisions of this
section in force immediately
before that commencement, then,
for the purposes of paragraph
(a) -

(i) such rights shall be

treated as rights in,
or arising out of,
research and
development the
expenditure on which
had been allowed as a
deduction in
ascertaining the
profits from the
trade, profession or
business under this
section; and

(ii) the reference in that
paragraph to the
amount of the
deduction in respect
of expenditure to
which such rights
relate shall be
construed as a
reference to the
aggregate of -

(A) the amount of
the deduction
allowed in
respect of
expenditure to
which such
rights relate
under the

provisions of
this section in
force

immediately
before that
commencement;
and

(B) the amount of
the deduction
allowed in
respect of
expenditure on
research and
development to
which such
rights relate
under this
section after
that
commencement." ;

(d) in subsection (4)(a) -

(i) in the definition of "an approved
research institute", by repealing
"scientific research" and substituting
"research and development";

(ii) by repealing the definition of
"scientific research" and substituting -

"research and development" (研究和開

發) means -

(a) any activities in

the fields of
natural or applied
science for the
extension of
knowledge;

(b) any systematic,
investigative or
experimental
activities carried
on for the purposes
of any feasibility
study or in relation
to any market,
business or
management research;

(c) any original and
planned
investigations
undertaken with the
prospect of gaining
new scientific or
technical knowledge
and understanding;
or

(d) the application of any
research findings or
other knowledge to a
plan or design for the
production or
introduction of new or

substantially improved materials, devices, products, processes, systems or services prior to the commencement of their commercial production or use.";

- (e) in subsection (5)(a) and (b), by repealing "scientific research" wherever it appears and substituting "research and development";
- (f) in subsection (6)(b), by repealing "scientific research" and substituting "research and development".

3. Home loan interest

Section 26E is amended -

- (a) in subsection (4)(c), by repealing "5 years" and substituting "7 years";
- (b) by adding -

"(10) For the avoidance of doubt, where any person has been allowed a deduction under the provisions of this section in force immediately before the commencement of section 3 of the Revenue Ordinance 2004 (of 2004), or has been regarded as having been allowed such deduction by virtue of section 26F(2)(b), for any year of assessment, that year of assessment shall be regarded as a year of assessment for which a deduction has been

allowed for the purposes of subsection (4)(c) as amended by section 3 of that Ordinance.".

4. Initial and annual allowances in respect of machinery and plant acquired under hire purchase agreement

Section 37A(4) is amended by repealing "scientific research" and substituting "research and development".

5. Interpretation

Section 40(1) is amended, in the definition of "industrial building or structure", in paragraph (f), by repealing "scientific research in relation" and substituting "research and development related".

Explanatory Memorandum

The purpose of this Bill is to amend the Inland Revenue Ordinance (Cap. 112) ("that Ordinance") to give effect to some of the proposals in the 2004-2005 Budget.

2. Clause 3 amends section 26E of that Ordinance to increase the number of years for which deductions for home loan interests paid by a person are allowable from 5 years of assessment to 7 years of assessment.

3. Clauses 2, 4 and 5 amend sections 16B, 37A and 40 of that Ordinance to replace references to "scientific research" with references to "research and development" and expand the scope of research and development activities expenditure on which is deductible for profits tax purpose.

Chapter:	112	INLAND REVENUE ORDINANCE	Gazette Number	Version Date
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Section:	16B	Expenditure on scientific research	32 of 1998	17/04/1998
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(1) Notwithstanding anything in section 17, in ascertaining the profits from any trade, profession or business in respect of which a person is chargeable to tax under this Part for any year of assessment there shall, subject to subsection (2), be deducted the following payments made, and expenditure incurred, by such person during the basis period for that year of assessment (other than any amount which is allowable as a deduction apart from this section), namely-

- (a) payments to-
 - (i) an approved research institute for scientific research related to that trade, profession or business; or
 - (ii) an approved research institute, the object of which is the undertaking of scientific research related to the class of trade, profession or business to which that trade, profession or business belongs; and
- (b) expenditure on scientific research related to that trade, profession or business, including capital expenditure except to the extent that it is expenditure on land or buildings or on alterations, additions or extensions to buildings.

(2) Where any payment or expenditure to which this section refers is made or incurred outside Hong Kong and the trade, profession or business in relation to which it is so made or incurred is carried on partly in and partly out of Hong Kong, the deduction allowable under this section shall be such part of the amount which would otherwise be allowable as is reasonable in the circumstances. (Amended 7 of 1986 s. 12)

- (3) (a) Where any plant or machinery, representing scientific research expenditure of a capital nature which pursuant to subsection (1)(b) has been allowed as a deduction in ascertaining the profits from a trade, profession or business, ceases to be used by the person carrying on the trade, profession or business for scientific research related to that trade, profession or business and is then or thereafter sold by him, the proceeds of sale shall, to the extent that they are not otherwise chargeable to tax under this Part and do not exceed the amount of the deduction, be treated as a trading receipt arising in or derived from Hong Kong of the trade, profession or business accruing at the time of the sale or, if the sale occurs on or after the date on which the trade, profession or business is permanently discontinued, accruing immediately before the discontinuance.
- (b) Where any such plant or machinery is destroyed, it shall for the purposes of paragraph (a) be treated as if it had been sold immediately before the destruction thereof and any insurance moneys or other compensation of any description received by the person carrying on the trade, profession or business in respect of the destruction and any money received by him in respect of the remains of the plant or machinery shall be treated as if they were proceeds of that sale.
- (c) The reference in paragraph (a) to the time of sale shall be construed as a reference to the time of completion or the time when possession is given, whichever is the earlier.

(3A)(a) Notwithstanding the exclusion relating to the sale of capital assets contained in section 14, where any rights in, or arising out of, scientific research the expenditure on which has been allowed as a deduction under this section in ascertaining the profits of any person from a trade, profession or business for the year of assessment commencing on 1 April 1998 or any subsequent year of assessment are thereafter sold by him-

- (i) subject to subparagraph (ii), the proceeds of sale;
- (ii) if the deduction has been allowed in accordance with subsection (2), such

- part of the proceeds of sale as is proportionate to the extent to which the expenditure on the scientific research to which the rights relate has been allowed as a deduction in accordance with that subsection,
- shall, to the extent that the proceeds of sale or the part of the proceeds of sale, as the case may be, is not otherwise chargeable to tax under this Part and does not exceed the amount of the deduction, be treated as a trading receipt of the trade, profession or business accruing at the time of the sale or, if the sale occurs on or after the date on which the trade, profession or business is permanently discontinued, accruing immediately before the discontinuance.
- (b) For the purposes of this subsection-
- (i) without prejudice to subsection (3), a reference to the proceeds of sale shall be construed as a reference to such part of the proceeds of sale as is not attributable to the sale of plant or machinery;
 - (ii) the reference to the time of the sale, in relation to any rights, shall be construed as a reference to the time of completion of the sale of the rights. (Added 32 of 1998 s. 7)
- (4) (a) In this section-
- "an approved research institute" (認可研究機構) means any university, college, institute, association or organization which is approved in writing for the purposes of this section by the Commissioner as an institute, association or organization for undertaking scientific research which is or may prove to be of value to Hong Kong; (Amended 7 of 1986 s. 12; 24 of 1996 s. 5)
- "scientific research" (科學研究) means-
- (a) any activities in the fields of natural or applied science for the extension of knowledge;
 - (b) any systematic, investigative or experimental activities carried on for the purposes of any feasibility study or in relation to any market, business or management research. (Replaced 32 of 1998 s. 7)
- (b) An approval for the purposes of paragraph (a) may-
- (i) operate as from a date, whether before or after the date of approval, specified in the instrument of approval; and
 - (ii) be withdrawn at any time.
- (5) In this section-
- (a) references to expenditure incurred on scientific research do not include any expenditure incurred in the acquisition of rights in, or arising out of, scientific research, but, save as aforesaid and subject to subsection (1)(b), include all expenditure incurred for the prosecution of, or the provision of facilities for the prosecution of, scientific research; and
 - (b) references to scientific research related to a trade, profession or business or class of trade, profession or business shall be read as including a reference to-
 - (i) any scientific research which may lead to or facilitate an extension, or an improvement in the technical efficiency, of that trade, profession or business, or, as the case may be, of trades, professions or businesses of that class; and
 - (ii) any scientific research of a medical nature which is of special relation to the welfare of workers employed in that trade, profession or business or, as the case may be, in trades, professions or businesses of that class; and
 - (c) a reference to rights shall be construed as including a reference to a share or interest in such rights. (Added 32 of 1998 s. 7)
- (6) For the purposes of this section-
- (a) expenditure shall not be regarded as incurred by a person in so far as it is, or is to be, met directly or indirectly by the Government of Hong Kong or by any government or public or local authority, whether in Hong Kong or elsewhere, or by any person other than the first-mentioned person; and (Amended 7 of 1986 s. 12; 19 of 1996 s. 5)

- (b) any expenditure of a capital nature incurred on scientific research related to any trade, profession or business by a person about to carry on that trade, profession or business shall be treated as if it had been incurred by that person on the first day upon which he does carry on that trade, profession or business.

(7) The same sums paid, or expenditure incurred, shall not be taken into account for any of the purposes of this section in relation to more than one trade, profession or business.

(Added 35 of 1965 s. 10. Amended 32 of 1998 s. 7)

Chapter:	112	INLAND REVENUE ORDINANCE	Gazette Number	Version Date
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Section:	26E	Home loan interest	31 of 1998	17/04/1998
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(1) Subject to the other provisions of this section and to section 26F, where a person pays during any year of assessment any home loan interest for the purposes of a home loan obtained in respect of a dwelling which is used at any time in that year of assessment by the person exclusively or partly as his place of residence, a deduction in respect of the home loan interest shall be allowable to that person for that year of assessment.

(2) (a) Subject to paragraphs (b) and (c) and subsection (3), a deduction allowable to a person under subsection (1) in respect of any home loan interest paid by the person during any year of assessment shall be-

(i) (A) where the dwelling is used by the person exclusively as his place of residence during the whole of that year of assessment, the amount of the home loan interest paid; or

(B) in any other case, such amount (whether representing the full amount of the home loan interest paid or any part thereof) as is reasonable in the circumstances of the case; or

(ii) the amount specified in Schedule 3D in relation to that year of assessment, whichever is of the lesser amount.

(b) For the purposes of this section, where a dwelling is held by a person otherwise than as a sole owner, the amount of the home loan interest paid referred to in paragraph (a)(i) shall be regarded as having been paid-

(i) where the dwelling is held by the person as a joint tenant, by the joint tenants each in proportion to the number of the joint tenants; or

(ii) where the dwelling is held by the person as a tenant in common, by the tenants in common each in proportion to his or her share in the ownership in the dwelling.

(c) For the purposes of paragraph (a), where a dwelling is held by a person otherwise than as a sole owner, the relevant amount specified in Schedule 3D referred to in paragraph (a)(ii) shall be regarded as having been reduced-

(i) where the dwelling is held by the person as a joint tenant, in proportion to the number of the joint tenants; or

(ii) where the dwelling is held by the person as a tenant in common, between the tenants in common each in proportion to his or her share in the ownership in the dwelling.

(3) (a) Where any home loan interest is paid by a person during any year of assessment for the purposes of a home loan obtained in respect of a dwelling which is used at any time in that year of assessment by that person exclusively or partly as his place of residence, but the loan was not applied wholly for the acquisition of the dwelling, the deduction allowable to the person under subsection (1) for that year

of assessment in respect of the home loan interest paid shall be such part of the amount of the home loan interest paid as is reasonable in the circumstances of the case.

- (b) Where any home loan interest is paid by a person during any year of assessment for the purposes of a home loan obtained in respect of a dwelling which is used at any time in that year of assessment by that person exclusively or partly as his place of residence, but the person has paid during that year of assessment any other home loan interest for the purposes of a home loan obtained in respect of any other dwelling which is also used at any time in that year of assessment by that person exclusively or partly as his place of residence, a deduction shall, subject to subsection (4), be allowable to the person under subsection (1) for that year of assessment in respect of both the first-mentioned home loan interest and the second-mentioned home loan interest, and the deduction so allowable shall be such amount (whether representing the full amount of the aggregate of the respective amounts of the first-mentioned home loan interest and the second-mentioned home loan interest or any part thereof) as is reasonable in the circumstances of the case.

(4) A deduction shall not be allowable under this section to a person in respect of any home loan interest paid during any year of assessment for the purposes of a home loan obtained in respect of a dwelling where-

- (a) the sum representing the home loan interest is allowable as a deduction under any other section of this Ordinance;
- (b) any other home loan interest paid in respect of any other dwelling has been allowed to the person as a deduction for that year of assessment under this section other than by virtue of subsection (3)(b); or
- (c) a deduction has been allowed to the person under this section, whether in respect of the same dwelling or in respect of any other dwelling, for 5 years of assessment (whether continuous or not).

(5) For the purposes of subsection (4)(c), where a deduction allowable to a person under this section has been taken into account in any year of assessment in ascertaining-

- (a) subject to paragraphs (b) and (c), the net chargeable income of the person;
- (b) where the person and his or her spouse have made an election under section 10(2), the aggregated net chargeable income of the person and his or her spouse; or
- (c) where the person or the person and his or her spouse have made an election under section 41, the amount of the assessment made under section 42A(1) in respect of the person or the person and his or her spouse,

the person shall be deemed to have been allowed the deduction under this section for that year of assessment.

- (6) (a) A claim by a person to a deduction allowable to him under this section may only be revoked by the person by notice in writing to the Commissioner within 6 months after the date on which the deduction is allowed to him under this section.
- (b) Where a claim is revoked under paragraph (a), the claim shall be deemed not to have been made.

(7) The Commissioner may, for the purposes of this section, approve in writing any organization or association as a recognized organization or association.

(8) For the purposes of this section, where a person pays any home loan interest for the purposes of a home loan obtained in respect of a dwelling which is used by that person exclusively or partly as his place of residence in the circumstances described in subsection (1), and the home loan was applied also for the acquisition of any car parking space valued together with the dwelling as a single tenement under section 10 of the Rating Ordinance (Cap 116), such car parking space shall be deemed-

- (a) to be part and parcel of the dwelling; and
- (b) to be used by that person in the same manner and to the same extent as the dwelling is used as his place of residence.

(9) In this section-

"dwelling" (住宅) means any building or any part of a building-

- (a) which is designed and constructed for use exclusively or partly for residential purposes; and
- (b) the rateable value of which is separately estimated under section 10 of the Rating Ordinance (Cap 116);

"home loan" (居所貸款), in relation to a person claiming a deduction under this section for any year of assessment, means a loan of money which is-

- (a) applied wholly or partly for the acquisition of a dwelling which-
 - (i) during any period of time in that year of assessment is held by the person as a sole owner, or as a joint tenant or tenant in common; and
 - (ii) during that period of time is used by the person exclusively or partly as his place of residence; and
- (b) secured during that period of time by a mortgage or charge over that dwelling or any other property in Hong Kong;

"home loan interest" (居所貸款利息), in relation to a person claiming a deduction in respect of a dwelling under this section, means interest paid by the person as a sole owner, or as a joint tenant or tenant in common of the dwelling for the purposes of a home loan to-

- (a) the Government;
- (b) a financial institution;
- (c) a credit union registered under the Credit Unions Ordinance (Cap 119);
- (d) a money lender licensed under the Money Lenders Ordinance (Cap 163);
- (e) the Hong Kong Housing Society;
- (f) an employer of the person; or
- (g) any recognized organization or association;

"place of residence" (居住地方), in relation to a person who has more than one place of residence, means his principal place of residence;

"recognized organization or association" (認可組織或協會) means any organization or association approved as such by the Commissioner under subsection (7).

(Added 31 of 1998 s. 12)

Chapter:	112	INLAND REVENUE ORDINANCE	Gazette Number	Version Date
Section:	37A	Initial and annual allowances in respect of machinery and plant acquired under hire-purchase agreement	32 of 1998 s. 22	17/04/1998

(1) Where a person carrying on a trade, profession or business incurs capital expenditure under a hire purchase agreement on the provision of machinery or plant for the purposes of producing profits chargeable to tax under Part IV then, except where such expenditure is expenditure of a kind described in section 16B(1)(b), there shall be made to him for each year of assessment in the basis period for which he has made an instalment payment under such agreement, an initial allowance. (Amended 35 of 1965 s. 20; 26 of 1969 s. 20; 23 of 1974 s. 3)

(1A) For the purposes of subsection (1), the initial allowance shall be-

- (a) in respect of a year of assessment up to and including the year of assessment commencing on 1 April 1973, equal to one-fifth of the capital portion only of the instalment payment referred to in subsection (1);
- (b) in respect of the year of assessment commencing on 1 April 1974 and all subsequent years of assessment up to and including the year of assessment

commencing on 1 April 1979, equal to one-quarter of the capital portion only of such payment;

- (c) in respect of the year of assessment commencing on 1 April 1980 equal to 35% of the capital portion only of such payment; and (Replaced 29 of 1982 s. 9)
- (d) in respect of the year of assessment commencing on 1 April 1981 and all subsequent years of assessment up to and including the year of assessment commencing on 1 April 1988, equal to 55% of the capital portion only of such payment. (Added 29 of 1982 s. 9. Amended 17 of 1989 s. 8)
- (e) in respect of any year of assessment commencing on or after 1 April 1989, equal to 60% of the capital portion only of such payment. (Added 17 of 1989 s. 8)

(2) Where at the end of the basis period for any year of assessment a person has in use for the purposes of producing profits chargeable to tax under Part IV, machinery or plant acquired by him under a hire purchase agreement there shall be made to him in respect of that year of assessment an annual allowance for depreciation by wear and tear on such machinery or plant. (Amended 26 of 1969 s. 20)

(3) An annual allowance under this section shall be calculated at rates prescribed by the Board of Inland Revenue and shall be computed on the reducing value of such machinery or plant which shall be the full cost thereof, excluding any interest which may be included in such cost under the terms of the agreement and reduced by any initial or previous annual allowances computed under this section: (Amended 35 of 1965 s. 20)

Provided that the Commissioner may in his discretion allow a higher rate than that prescribed by the Board of Inland Revenue.

(4) Nothing in subsection (2) shall apply in respect of any machinery or plant used by a person for the purposes of his trade, profession or business where such machinery or plant represents scientific research expenditure of a capital nature which pursuant to section 16B(1)(b) has been allowed as a deduction in ascertaining the profits from such trade, profession or business in respect of which such person is chargeable to tax under Part IV for any year of assessment. (Added 35 of 1965 s. 20. Amended 32 of 1998 s. 22)

(Added 36 of 1955 s. 43)

Chapter:	112	INLAND REVENUE ORDINANCE	Gazette Number	Version Date
Section:	40	Interpretation	32 of 1998	17/04/1998

(1) In this Part-
"basis period" (評稅基期) has the meaning assigned to it by section 2 except that-

- (a) where 2 basis periods overlap the period common to both shall be deemed to fall in the first basis period only, and
- (b) where there is an interval between the end of the basis period for one year of assessment and the beginning of the basis period for the next year of assessment the interval shall be deemed to fall in the second basis period but where, in respect of salaries tax, the interval is the year ending on 31 March 1973, that interval shall not be deemed to fall in the second basis period; (Replaced 49 of 1956 s. 28. Amended 8 of 1973 s. 8)

"capital expenditure" (資本開支)-

- (a) includes interest paid and commitment fees incurred in respect of a loan made for the sole purpose of financing the provision of an industrial building or structure or commercial building or structure or machinery or plant; but
- (b) does not include expenditure which is reimbursed by way of or attributable to any grant, subsidy or similar financial assistance and in relation to the person incurring

the expenditure does not include any expenditure which is allowed to be deducted in ascertaining for the purpose of Part IV the profits of a trade, profession or business carried on by that person; (Replaced 30 of 1981 s. 7. Amended 32 of 1998 s. 25)

"capital expenditure on the provision of machinery or plant" (在提供機械或工業裝置方面的資本開支) includes capital expenditure on alterations to an existing building incidental to the installation of that machinery or plant for the purposes of the trade, profession or business;

"class of machinery or plant" (該類機械或工業裝置、類別的機械或工業裝置) means the items of machinery or plant for which the same rate of depreciation is prescribed by the Board of Inland Revenue; (Added 63 of 1980 s. 4)

"commercial building or structure" (商業建築物或構築物) means any building or structure or part of any building or structure used by the person entitled to the relevant interest for the purposes of his trade, profession or business other than an industrial building or structure; (Replaced 35 of 1965 s. 22. Amended 26 of 1969 s. 22)

"industrial building or structure" (工業建築物或構築物) means any building or structure or part of any building or structure used-

- (a) for the purposes of a trade carried on in a mill, factory or other similar premises; or
- (b) for the purposes of a transport, tunnel, dock, water, gas or electricity undertaking or a public telephonic or public telegraphic service; or (Amended 39 of 1969 s. 5)
- (c) for the purposes of a trade which consists of the manufacture of goods or materials or the subjection of goods or materials to any process; or
- (d) for the purposes of a trade which consists in the storage-
 - (i) of goods or materials which are to be used in the manufacture of other goods or materials; or
 - (ii) of goods or materials which are to be subjected in the course of a trade to any process; or
 - (iii) of goods or materials on their arrival into Hong Kong; or (Amended 7 of 1986 s. 12)
- (e) for the purposes of the business of farming;
- (f) for the purposes of scientific research in relation to any trade, profession or business, (Amended 32 of 1998 s. 25)

and, in particular, the said expression includes any building or structure or part of any building or structure used by a person carrying on a trade, undertaking or business specified in paragraphs (a) to (e) of this definition and provided by him for the welfare of workers employed in his trade, undertaking or business and in use for that purpose:

Provided that-

- (i) where part of the whole of a building or structure is, and part thereof is not, an industrial building or structure, and the capital expenditure which has been incurred on the construction of the second mentioned part is not more than one-tenth of the total capital expenditure which has been incurred on the construction of the whole building or structure, the whole building or structure and every part thereof shall be treated as an industrial building or structure; and
- (ii) subject to the provisions of paragraph (i) of this proviso but notwithstanding anything else contained in the foregoing provisions of this definition, the expression "industrial building or structure" (工業建築物或構築物) shall not include any building or structure or part of any building or structure used as a dwelling house (other than as a dwelling house for the housing of manual workers), retail shop, showroom, hotel or office; (Replaced 35 of 1965 s. 22)

"relevant interest" (有關權益) means, in relation to any expenditure incurred on the construction of a building or structure the interest in that building or structure to which the person who incurred the expenditure was entitled when he incurred it; (Amended 49 of 1956 s. 28)

"residue of expenditure" (開支剩餘額)-

- (a) in relation to a commercial building or structure, means the amount of the capital expenditure incurred on the construction of the building or structure reduced by-
- (i) the amount of any annual allowance made under section 33A;
 - (ii) the amount of any balancing allowance made under section 33B,
- and increased by any balancing charges made under section 33B:

Provided that in computing the residue of expenditure there shall be written off, in respect of any year in which no annual allowance fell to be made under section 33A, an amount of one-twenty-fifth of the capital expenditure, and for the purposes of this proviso "year" (年) means the period which would have comprised a year of assessment commencing on 1 April 1998 or any subsequent year of assessment in respect of which an annual allowance would have fallen to be made under section 33A if the building or structure had been in use as a commercial building or structure; (Added 32 of 1998 s. 25)

- (b) in relation to an industrial building or structure, means the amount of the capital expenditure incurred on the construction of the building or structure reduced by-
- (i) the amount of any initial allowance made under section 34(1);
 - (ii) any annual allowance made under section 34(2);
 - (iii) any balancing allowance made under section 35,
- and increased by any balancing charges made under section 35:

Provided that in computing the residue of expenditure there shall be written off, in respect of any year in which no initial or annual allowance fell to be made under section 34(1) or (2), as the case may be, an amount of one-fiftieth of the capital expenditure in the case of a year prior to the year of assessment commencing on 1 April 1965, and one-twenty-fifth of the capital expenditure in the case of such or any subsequent year of assessment, and for the purposes of this proviso "year" (年) means the period which would have comprised a year of assessment in respect of which an initial or annual allowance would have fallen to be made under section 34(1) or (2), as the case may be, if the building or structure had then been in use as an industrial building or structure and the provisions of section 34 had then been in force. (Replaced 35 of 1965 s. 22. Amended 32 of 1998 s. 25)

(2) For the purposes of this Part, any capital expenditure incurred for the purposes of a trade, profession or business by a person about to carry on such trade, profession or business shall be treated as if it had been incurred by that person on the first day upon which he does carry on such trade, profession or business. (Added 35 of 1965 s. 22)

(3) References in this Part to capital expenditure incurred on the construction of a building or structure do not include any expenditure incurred on the acquisition of, or of rights in or over, any land. (Added 29 of 1982 s. 11)

(Replaced 36 of 1955 s. 46)