

**立法會**  
**Legislative Council**

LC Paper No. CB(1)1668/12-13  
(These minutes have been seen  
by the Administration)

Ref : CB1/BC/2/12

**Bills Committee on Inland Revenue and Stamp Duty Legislation  
(Alternative Bond Schemes) (Amendment) Bill 2012**

**First meeting on  
Tuesday, 29 January 2013, at 2:30 pm  
in Conference Room 2A of the Legislative Council Complex**

**Members present** : Hon CHAN Kam-lam, SBS, JP (Chairman)  
Hon Abraham SHEK Lai-him, SBS, JP  
Hon Ronny TONG Ka-wah, SC  
Hon Starry LEE Wai-king, JP  
Hon Kenneth LEUNG  
Hon Christopher CHEUNG Wah-fung, JP  
Hon SIN Chung-kai, SBS, JP

**Public officers attending** : Miss Salina YAN, JP  
Deputy Secretary for Financial Services and  
the Treasury (Financial Services) 1

Mr Jackie LIU  
Principal Assistant Secretary for Financial Services and  
the Treasury (Financial Services) 5

Mr Daryl HO  
Head, Market Development Division  
Hong Kong Monetary Authority

Ms Carrie CHAN  
Senior Manager (Market Development)  
Hong Kong Monetary Authority

Mr WONG Kuen-fai, JP  
Deputy Commissioner (Operations)  
Inland Revenue Department

Mr Allen NG  
Senior Assessor (Research)  
Inland Revenue Department

Ms Betty CHEUNG  
Senior Assistant Law Draftsman  
Department of Justice

Mr Manuel NG  
Government Counsel  
Department of Justice

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

**Staff in attendance** : Mr KAU Kin-wah  
Senior Assistant Legal Adviser 3

Mr Hugo CHIU  
Council Secretary (1)4

Ms Sharon CHAN  
Legislative Assistant (1)4

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## **I Election of Chairman**

Mr CHAN Kam-lam, the member with the highest precedence among those present at the meeting, presided over the election of the Chairman of the Bills Committee. He invited nominations for the chairmanship of the Bills Committee.

2. Mr CHAN Kam-lam was nominated by Ms Starry LEE and the nomination was seconded by Mr Christopher CHEUNG. Mr CHAN Kam-lam accepted the nomination. Mr Kenneth LEUNG was nominated by Mr SIN Chung-kai. The nomination was invalid as it was not seconded by another member. There being no other nomination, Mr CHAN Kam-lam was elected Chairman of the Bills Committee.

3. Members agreed that there was no need to elect a Deputy Chairman.

Declaration of interests

4. Ms Starry LEE declared that the company she worked for might engage in consultation services on taxation matters but she was not involved in the business. Mr Kenneth LEUNG declared that he was engaged in consultation services on taxation and Islamic finance matters. Mr Christopher CHEUNG declared that his company might be involved in the trading of Islamic bonds.

**II Meeting with the Administration**

- (LC Paper No. CB(3)264/12-13 -- The Bill
- LC Paper No. CB(1)480/12-13(01) -- Marked-up copy of the Bill prepared by the Legal Service Division (Restricted to Members)
- File Ref: B9/33/2C -- Legislative Council Brief
- LC Paper No. LS16/12-13 -- Legal Service Division Report
- LC Paper No. CB(1)480/12-13(02) -- Background brief on the Inland Revenue and Stamp Duty Legislation (Alternative Bond Schemes) (Amendment) Bill 2012 prepared by the Legislative Council Secretariat)

5. The Bills Committee deliberated (Index of proceedings attached at **Appendix**).

Admin Follow-up actions to be taken by the Administration

6. The Administration was requested to provide the following information:
  - (a) highlights of the public consultation on the proposed amendments to the Inland Revenue Ordinance (Cap. 112) and the Stamp Duty Ordinance (Cap. 117) to facilitate development of an Islamic bond market in Hong Kong (conducted in March 2012), and the consultation conclusions (released in October 2012) including the Administration's responses to the comments and suggestions received during the consultation;

- (b) tax law reforms in other jurisdictions, including the United Kingdom, Japan, Singapore and Malaysia, to facilitate the development of Islamic bond market, covering areas including the approach taken in the reforms, types of sukuk, tax treatment, provision of other types of tax reliefs or incentives, etc.; and
- (c) the issuance of and investment in sukuk in the Mainland financial market in recent years, including the major sukuk issuers and investment in sukuk by China Investment Corporation and other sovereign wealth funds operating in the Mainland

### **III Any other business**

#### Invitation for views

7. Members agreed to receive deputations' views on the Bill. According to the usual practice, an invitation notice would be posted on the Legislative Council website to invite public views on the Bill. The District Councils and relevant organizations would be invited to provide written submissions and attend the public hearing.

*(Post-meeting note: A list of organizations to be invited for written submissions and attendance of the public hearing was issued on 5 February 2013 vide LC Paper No. CB(1) 528/12-13.)*

#### Date of next meeting

- 8. Members agreed that the next meeting would be held on Monday, 18 March 2013, at 9:00 am to meet with deputations and the Administration.
- 9. There being no other business, the meeting ended at 3:51 pm.

Council Business Division 1  
Legislative Council Secretariat  
7 August 2013

**Proceedings of the  
Bills Committee on Inland Revenue and Stamp Duty Legislation  
(Alternative Bond Schemes) (Amendment) Bill 2012  
First meeting on Tuesday, 29 January 2013, at 2:30 pm  
in Conference Room 2A of the Legislative Council Complex**

Time Marker	Speaker	Subject(s)	Action Required
000219 – 000442	Mr CHAN Kam-lam Ms Starry LEE Mr Christopher CHEUNG Mr SIN Chung-kai Mr Kenneth LEUNG	Election of Chairman	
000443 – 000555	Ms Starry LEE Mr Kenneth LEUNG Mr Christopher CHEUNG	Declaration of interest by members	
000556 – 000640	Chairman	Introductory remark	
000641 – 002953	Administration	Briefing by the Administration on the Inland Revenue and Stamp Duty Legislation (Alternative Bond Schemes) (Amendment) Bill 2012 ("the Bill") (Powerpoint material issued vide Lotus Notes e-mail on 30 January 2013)	
002954 – 003654	Ms Starry LEE Administration	<p>Ms LEE enquired about:</p> <p>(a) the characteristics of Islamic bonds ("sukuk") and their attractiveness vis-à-vis conventional bonds; and</p> <p>(b) whether investors of sukuk would be Muslims only.</p> <p>The Administration responded as follows:</p> <p>(a) Owing to the need to comply with the principles of Islamic law (known as "Shariah") which prohibited receipts and payments of interests, sukuk were asset-backed or asset-based instruments instead of debt-based instruments that paid interests.</p> <p>(b) Sukuk were purchased by both Muslims and non-Muslims investors.</p>	

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		<p>(c) Substantial growth in the demand of sukuk in recent years could be attributed to the strong financing needs of Islamic economies due to their rapid economic development, the lower risks of sukuk as perceived by investors compared to government or corporate bonds issued by some developed economies, growth in assets possessed by oil-producing countries and assets generated from Islamic banking system both looked for investment opportunities in sukuk.</p>	
003655 – 004813	Mr SIN Chung-kai Administration	<p>Mr SIN pointed out that the use of the term "Alternative Bond Schemes" ("ABS") instead of "sukuk" in the Bill might not draw the attention of market participants on the taxation framework and might affect the effectiveness to facilitate the development of a local sukuk market. He enquired about the reasons for adopting a religion-neutral approach in drafting the Bill, the feedbacks received during the public consultation conducted in March 2012 in this regard, and the drafting approach of the sukuk-related legislation of other common law jurisdictions.</p> <p>The Administration responded as follows:</p> <p>(a) Other jurisdictions like the United Kingdom ("UK") adopted a religion-neutral approach in the relevant law for sukuk. Major jurisdictions had amended their tax laws to facilitate the issuance of sukuk. While a direct comparison of the legislation might not be appropriate owing to the unique circumstances of individual jurisdictions, the coverage of the Bill was relatively more comprehensive than other relevant jurisdictions. For instance, the Bill covered five types of sukuk while the legislation of other relevant jurisdictions like the UK, Singapore and Japan covered Ijarah only.</p> <p>(b) The draft provisions included in the Bill was set out in a consultation paper issued for public consultation in March 2012. The religion-neutral approach was generally accepted by the market. The</p>	

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		<p>consultation did not indicate any difficulty from market participants in understanding the application of the Bill.</p> <p>(c) The Administration had taken on board a number of suggestions and comments from the market in finalizing the Bill, such as expansion on the coverage of investment arrangements to include Wakalah, extension of the "maximum term length" condition (one of the qualifying conditions for a specified ABS to be given the proposed tax treatment) from ten years to 15 years, and shortening of the record-keeping period for the relevant documents.</p> <p>(d) If necessary, the Administration would extend the coverage of ABS to include new types of sukuk in the future. The Administration was aware of the need to set out the major features of each type of sukuk to facilitate the understanding of the public and investors as well as the assessment work of the Inland Revenue Department ("IRD"). The Administration would work with the regulators including the Hong Kong Monetary Authority on enhancing investor education as appropriate.</p> <p>The Administration was requested to provide the following information:</p> <p>(a) highlights of the public consultation conducted in March 2012, and the consultation conclusions (released in October 2012) including the Administration's responses to the comments and suggestions received during the consultation; and</p> <p>(b) tax law reforms in other jurisdictions, including the UK, Japan, Singapore and Malaysia, to facilitate the development of Islamic bond market, covering areas including the approach taken in the reforms, types of sukuk, tax treatment, provision of other types of tax reliefs or incentives, etc.</p>	<p>The Administration to take action as per paragraph 6(a) and (b) of the minutes</p>

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		<p>Mr SIN remarked that the Bills Committee should hear the views of deputations and public on the Bill.</p>	
<p>004814 – 005638</p>	<p>Mr Kenneth LEUNG Administration</p>	<p>Mr LEUNG enquired and was concerned about:</p> <ul style="list-style-type: none"> <li>(a) the amount of sukuk issued in 2011 and 2012 in the Hong Kong market;</li> <li>(b) the number and results of applications for profits tax, property tax and stamp duty exemption for sukuk issuance and transactions made under section 87 of the Inland Revenue Ordinance ("IRO") and section 52 of the Stamp Duty Ordinance ("SDO");</li> <li>(c) the number of banks in Hong Kong with Islamic banking windows or Islamic banking desks; and</li> <li>(d) whether the lack of references to prohibited activities under Shariah (like gambling and the making of pork-related products) in the Bill would affect the implementation of the Bill.</li> </ul> <p>The Administration responded as follows:</p> <ul style="list-style-type: none"> <li>(a) There were two main channels for sukuk offering: listing on the Stock Exchange of Hong Kong ("SEHK") or private placement. A total of six sukuk with tenor ranging from five to ten years and amounted to US\$5.8 billion were listed on SEHK in the past six years. There were no official statistics on the size of private placement of sukuk, and it was believed that the buyers were mainly institutional and professional investors.</li> <li>(b) The Administration had processed an application for profits tax exemption and another application for stamp duty exemption for sukuk issuance and transactions made under section 87 of IRO and section 52 of SDO respectively. One application for stamp duty exemption was being processed. Due to the need to</li> </ul>	



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		<p>observe rules of confidentiality, the Administration could not disclose details of these applications.</p> <p>(c) The local subsidiaries of two banks from Malaysia had launched Islamic banking windows in Hong Kong.</p> <p>(d) As the Bill was to amend IRO and SDO to provide for a comparable taxation framework for some common types of sukuk vis-à-vis conventional bonds, the Bill had adopted a religion-neutral drafting approach by focusing on the major features of sukuk essential for determination of tax liability without importing detailed requirements under Shariah. An issuer of sukuk would need to structure their products in accordance with relevant Islamic principles in order to market those products to a particular segment of investors bound by these principles.</p> <p>Mr LEUNG supported the suggestion for the Bills Committee to hear the views of deputations and public on the Bill.</p>	
005639 – 010833	Ms Starry LEE Administration Chairman	<p>Ms LEE concurred with Mr SIN Chung-kai's view regarding the references to ABS vis-à-vis "sukuk" in the Bill. She enquired about:</p> <p>(a) the reasons for the rapid growth of Islamic finance; and</p> <p>(b) the offering procedures and requirements of sukuk and measures to protect sukuk investors having regard to the experience of the Lehman Brothers Incident.</p> <p>The Administration replied as follows:</p> <p>(a) Rapid expansion in global Islamic finance was the results of strong financing needs of Islamic economies owing to their rapid economic development, and the assessment of some investors that sukuk involved lower risks than conventional bonds issued in some developed economies.</p>	

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		<p>(b) Hong Kong's advantages in the development of a sukuk market included its highly liquid capital market and the huge potential in the development of offshore Renminbi ("RMB") business. An array of RMB-denominated Islamic financial products already existed in the financial markets.</p> <p>(c) The market had reflected to the Administration about the absence of a comparable taxation framework that catered for the issuance of sukuk vis-à-vis that of conventional bonds. The relatively small number of applications for profits tax and stamp duty exemption for sukuk issuance and transactions in the past might be evidence of market's concern about the lack of relevant legal framework and infrastructure for the development of Islamic finance in Hong Kong.</p> <p>(d) Similar to other financial products, products offered under ABS would be subject to the prevailing regulatory regime in respect of product offering, marketing, disclosure and intermediaries requirements in accordance with relevant provisions of the Securities and Futures Ordinance (Cap. 571) ("SFO") and the Companies Ordinance (Cap. 32) ("CO").</p> <p>(e) The Administration and the regulators would step up efforts on investor education as appropriate.</p> <p>Ms LEE and the Chairman enquired about the operation of sukuk and protection for sukuk investors given that sukuk had more complicated features and structures than conventional bonds.</p> <p>The Administration responded as follows:</p> <p>(a) While sukuk would be structured in ways to comply with Shariah, the majority of sukuk operated like conventional bonds in practice. In general, most sukuk were purchased by institutional investors. Similar to conventional bonds, sukuk would specify their coupon rates.</p>	

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		<p>(b) The term ABS instead of sukuk was used in the Bill because the Bill was to amend IRO and SDO to provide for a comparable taxation framework for some common types of sukuk, vis-à-vis conventional bonds. As target users of the Bill were institutions structuring sukuk in the market, the existing drafting of the Bill could provide a clear legal framework for such users for taxation purposes. Investors should rely on the offering documents to assess the relevant parameters of specific sukuk products, e.g. the underlying investment arrangements.</p>	
010834 – 011055	Chairman Administration	<p>The Chairman enquired about the protection for sukuk investors in the event that the sukuk concerned had failed to meet the qualifying conditions for the proposed tax treatment. He was concerned that when a sukuk become no longer entitled for the proposed tax treatment, its operating costs would be higher and there would be higher chance of default.</p> <p>The Administration clarified that the qualifying conditions were only relevant to the eligibility for the proposed tax treatment under the Bill and had nothing to do with the default, if any, of the sukuk. Any failure for the sukuk to meet the qualifying conditions would not necessarily lead to default of the concerned sukuk. The offering documents of sukuk would specify the circumstances leading to the event of default. The purpose of the Bill was not to provide for the regulation of the issuance of sukuk which would be subject to provisions in SFO and CO as appropriate.</p>	
011056 – 011331	Mr Kenneth LEUNG Administration	<p>Mr LEUNG enquired whether the failure of a sukuk in meeting the qualifying conditions would affect the coupon rate and investment returns of the sukuk.</p> <p>The Administration responded that the coupon rates of sukuk were market driven. The offering documents of sukuk would specify the coupon rates. There were clauses to expressly disclose the risk of the investments when the product was offered to the investing public.</p>	

Time Marker	Speaker	Subject(s)	Action Required
		Mr LEUNG requested the Administration to provide information on the issuance of and investment in sukuk in the Mainland financial market in recent years, including the major sukuk issuers and investment in sukuk by China Investment Corporation and other sovereign wealth funds operating in the Mainland.	The Administration to take action as per paragraph 6(c) of the minutes.
011332 – 011804	Ms Starry LEE Administration Chairman	<p>Ms LEE enquired about the issuance requirements of sukuk and the handling of legal disputes relating to sukuk.</p> <p>The Administration's responses as follows:</p> <p>(a) Similar to other financial products, sukuk were subject to the prevailing regulatory regime in respect of product offering, marketing, disclosure and intermediaries requirements in accordance with relevant provisions of SFO and CO.</p> <p>(b) In general, an issuer of sukuk would ensure that the sukuk were structured in Shariah-compliant ways. The offering documents of sukuk would specify the governing law of the sukuk in the event of legal disputes relating to the product.</p> <p>The Chairman remarked that the issuer of sukuk might not necessarily be an Islamic institution.</p>	
011805 – 011950	Mr Kenneth LEUNG Administration	In response to Mr LEUNG's enquiry, the Administration advised that details of record keeping requirements were set out in footnote 13 of the Legislative Council Brief of the Bill.	
011951 – 012224	Chairman	Date and arrangements for holding a meeting to hear views from deputations and public on the Bill.	