

立法會
Legislative Council

LC Paper No. CB(1)1269/13-14
(These minutes have been seen
by the Administration)

Ref : CB1/BC/3/13

Bills Committee on Inland Revenue (Amendment) (No. 3) Bill 2013

First meeting on
Tuesday, 28 January 2014, at 10:45 am
in Conference Room 2A of the Legislative Council Complex

Members present : Hon WONG Ting-kwong, SBS, JP (Chairman)
Hon James TO Kun-sun
Hon CHAN Kam-lam, SBS, JP
Hon Andrew LEUNG Kwan-yuen, GBS, JP
Hon CHAN Kin-por, BBS, JP
Hon Alan LEONG Kah-kit, SC
Hon Charles Peter MOK
Hon Kenneth LEUNG
Hon SIN Chung-kai, SBS, JP

Member absent : Hon Starry LEE Wai-king, JP

Public officers attending : Mr Eddie CHEUNG
Deputy Secretary for Financial Services and the
Treasury (Financial Services) 2

Mr CHIU Kwok-kit, JP
Deputy Commissioner of Inland Revenue (Technical)

Mr Tony CHAN
Acting Assistant Commissioner of Insurance
(Policy and Development)

Mr Manuel NG
Acting Senior Government Counsel
Department of Justice

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

Staff in attendance : Mr Timothy TSO
Assistant Legal Adviser 2

Ms Angel SHEK
Senior Council Secretary (1)4

Ms Sharon CHAN
Legislative Assistant (1)4

Action

I Election of Chairman

Election of Chairman

Mr CHAN Kam-lam, the member with the highest precedence among those who were 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 WONG Ting-kwong was nominated by Mr Andrew LEUNG and the nomination was seconded by Mr CHAN Kin-por. Mr WONG Ting-kwong accepted the nomination. There being no other nomination, Mr WONG was elected the Chairman of the Bills Committee.

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

Application for late membership

4. The Chairman informed members of the application from Mr Charles Peter MOK for late membership of the Bills Committee. Members agreed to accept Mr MOK as a member of the Bills Committee.

II Meeting with the Administration

- (LC Paper No. CB(3)291/13-14 — The Bill
- LC Paper No. CB(1)790/13-14(01) — Marked-up copy of the Bill prepared by the Legal Service Division (Restricted to Members)
- File Ref: L/M (19) in G6/90/4C (2011) Pt. 5 — Legislative Council Brief
- LC Paper No. LS22/13-14 — Legal Service Division Report
- LC Paper No. CB(1)790/13-14(02) — Background brief on Inland Revenue (Amendment) (No. 3) Bill 2013 prepared by the Legislative Council Secretariat)

5. Mr Kenneth LEUNG declared that his work involved advising on tax matters but did not include the business of captive insurers.

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

Follow-up actions to be taken by the Administration

Proposed profits tax concession for captive insurers

7. With regard to the proposed profits tax concession for captive insurers, the Administration was requested to provide information/response to members' views as follows –

- (a) the rationale for setting the proposed profits tax rate at one-half of the normal tax rate for corporations which was currently 16.5%;
- (b) the reasons for only applying the proposed concessionary profits tax rate to captive insurers pertaining to their business of insurance and reinsurance of offshore risks but not onshore risks;
- (c) comparison of the proposed concessionary profits tax rate and other regulatory concessions granted to captive insurers by Hong Kong and other jurisdictions; and explain how Hong Kong would maintain its competitiveness in attracting captive insurers vis-à-vis other jurisdictions;

- (d) whether the proposed tax concession was targeted at attracting captive insurers from particular jurisdictions, such as the Mainland, to establish in Hong Kong; and
- (e) some members' views that the Administration should make reference to other jurisdictions to exempt captive insurers from all profits tax (e.g. Singapore) or exempt them from such tax in the first two years of their operation in Hong Kong.

Definition of captive insurance business eligible for the proposed tax concessions

8. According to section 2(7) of the Insurance Companies Ordinance (Cap. 41) ("ICO"), captive insurer was defined as an insurer which carried on general business only and was restricted to underwriting insurance and reinsurance of risks of the companies within the same grouping of companies to which the captive insurer belonged. The same grouping of companies to which the captive insurer belonged might cover a company which the captive insurer or any company belonging to the same group held, or was entitled to control the exercise of; not less than 20% of the voting power at any general meeting. In providing the proposed concessionary profits tax rate for captive insurers, the Administration was requested to –

- (a) explain the appropriateness to adopt the definition of "same grouping of companies" under ICO for the purpose of the proposed tax concessions, having regard to the concern that the percentage of controlling stake (i.e. not less than 20%) in question might be over generous and had implications on tax revenue;
- (b) provide information on the definition of "same grouping of companies" or other relevant definitions adopted by other jurisdictions for the purpose of granting profits tax concessions to captive insurers; and
- (c) consider the need to provide a definition of "offshore risks" in the Bill, with reference to major tax cases in other jurisdictions involving disputes/loopholes over the scope of "offshore risks".

Section 39E of the Inland Revenue Ordinance (Cap. 112) ("IRO")

9. In light of the proposed tax concessions for captive insurance business of offshore risks, the Administration was requested to respond to some members' views that similar considerations should be given to relaxing the restrictions

under section 39E of IRO to grant depreciation allowances to a Hong Kong enterprise if the machinery or plants owned by the enterprise were used wholly or principally outside Hong Kong by another enterprise under a leasing arrangement.

Drafting issue

10. In light of comments of the Legal Adviser to the Bills Committee, the Administration was requested to explain the drafting of sections 2(2), 2(4), 4(2) and 4(4) of the proposed Schedule 30 to IRO with regard to the usage of "the ground is..." (English text) and "有關理由是" (Chinese text), which seemed to depart from the drafting of similar provisions in other parts of IRO (e.g. existing section 3(4) of Schedule 25).

III Any other business

Invitation of views

11. Members agreed that it was unnecessary for the Bills Committee to invite the public or relevant parties to give views on the Bill.

Way forward

12. The Chairman concluded that the Bills Committee had completed scrutiny of the Bill. Members agreed that the Administration be invited to provide written response on the follow-up actions which would be circulated to members. Subject to views members might have on the Administration's written response, the Chairman would decide whether it was necessary to hold a further meeting.

(Post-meeting note: The Administration's written response was issued to members on 14 February 2014 vide LC Paper No. CB(1)905/13-14. At the request of Hon James TO and on the instruction of the Chairman, a further meeting of the Bills Committee was held on 24 February 2014, at 10:45 am to discuss the Administration's response. The notice of meeting was issued on 20 February 2014 vide LC Paper No. CB(1)952/13-14.)

13. There being no other business, the meeting ended at 12:10 pm.

**Proceedings of the
Bills Committee on Inland Revenue (Amendment) (No. 3) Bill 2013
First meeting on Tuesday, 28 January 2014, at 10:45 am
in Conference Room 2A of the Legislative Council Complex**

Time Marker	Speaker	Subject(s)	Action Required
000132 – 000335	Mr CHAN Kam-lam Mr Andrew LEUNG Mr CHAN Kin-por Mr WONG Ting-kwong	Election of Chairman	
000336 – 000359	Chairman	Members accepted Mr Charles MOK's application for late membership of the Bills Committee	
000400 – 000814	Chairman Administration	Briefing by the Administration on the Inland Revenue (Amendment) (No. 3) Bill 2013 ("the Bill") (Legislative Council Brief (File Ref: L/M (19) in G6/90/4C (2011) Pt. 5))	
000815 – 001549	Chairman Mr Andrew LEUNG Administration	<p>Mr LEUNG expressed support for granting tax concessions for captive insurers' business of insurance of offshore risks. He pointed out that the same principle should apply to the case where a Hong Kong enterprise engaging in "import processing" arrangements in leasing its machinery or plant to an enterprise outside Hong Kong which belonged to the same group of companies of the Hong Kong enterprise. Hence, he opined that similar consideration should be given to relaxing the restrictions under section 39E of the Inland Revenue Ordinance (Cap. 112) ("IRO") in order to allow Hong Kong enterprises engaging in "import processing" arrangements to claim depreciation allowances for machinery or plant made available for use by the Mainland enterprises rent-free.</p> <p>The Administration considered that there were no justifiable grounds to relax the existing restriction in section 39E of IRO given Hong Kong's established taxation principles of "territorial source" and "tax symmetry", as well as the problem of transfer pricing. According to the "territorial source" principle, profits tax would not be charged on Hong Kong enterprises in relation to Mainland enterprises' production activities. Based on the "tax</p>	The Administration to take action as per paragraph 9 of the minutes.

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		<p>symmetry" principle, depreciation allowances for the machinery or plant used by the Mainland enterprises in their production activities would not be granted. From the international perspective, the tax authorities around the world (including the State of Administration of Tax of China) are all increasingly concerned about the transfer pricing issue arising from cross-border trading activities between associated enterprises.</p>	
001550 – 002238	Chairman Mr CHAN Kam-lam Administration	<p>Mr CHAN enquired about the reasons for applying the proposed concessionary profits tax rate to captive insurers' business of <u>offshore risks only</u> but not onshore risks as well; the projected growth in the number of captive insurers domiciled in Hong Kong; and impact on tax revenue as a result of the proposed tax concession.</p> <p>The Administration responded that –</p> <p>(a) the proposal had taken into account the unique development of captive insurance business in Hong Kong and the profits tax concession currently applicable to reinsurance companies for their business of offshore risks only. The Administration would continue to keep under review the impact on tax revenue and the need for further measures to promote insurance business in Hong Kong in light of market developments; and</p> <p>(b) there were currently two captive insurers in Hong Kong. The proposal would attract companies to set up captive insurers in Hong Kong and help the development of other related businesses, including reinsurance, legal and actuarial services, etc., as well as reinforce Hong Kong's status as a regional insurance hub. However, it was difficult to project the growth in captives due to the tax concession measure at this stage.</p>	<p>The Administration to take action as per paragraph 7(b) of the minutes.</p>

Time Marker	Speaker	Subject(s)	Action Required
002239 – 002956	Chairman Mr James TO Administration	<p>Mr TO enquired about –</p> <ul style="list-style-type: none"> (a) the rationale for setting the proposed profits tax rate at one-half of the normal tax rate; (b) whether the proposed tax concession was targeted at attracting captive insurers from particular jurisdictions, such as the Mainland, in light of the relevant policy promulgated by the State Council in June 2012 ("the State Council's policy"); and (c) comparison of the proposed concessionary profits tax rate and other regulatory concessions granted to captive insurers by Hong Kong and other jurisdictions; and how Hong Kong would maintain its competitiveness in attracting captive insurers vis-à-vis other jurisdictions. <p>The Administration advised that –</p> <ul style="list-style-type: none"> (a) the proposal was a positive response to the insurance industry's suggestion that Hong Kong should consider offering tax concessions to attract enterprises to choose Hong Kong as the domicile for captive insurers. This suggestion had been made before promulgation of the State Council's policy. The proposal was meant to attract captive insurers from around the world (not just from the Mainland) to domicile in Hong Kong; and (b) profits tax on captive insurers' offshore business was currently waived in Singapore and Bermuda, whereas no profits tax was imposed for captive insurers' business in Qatar. The concessionary profits tax rates for captive insurance business in Delaware of the United States ranged from 0.1% to 0.2% depending on the types of businesses. The profits tax in Labuan of Malaysia was 3%. 	

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		<p>At the request of the Chairman and Mr TO, the Administration undertook to provide a written response to Mr TO's enquiries above.</p>	<p>The Administration to take action as per paragraph 7(a), (c) and (d) of the minutes.</p>
<p>002957 – 004227</p>	<p>Chairman Mr Kenneth LEUNG Mr CHAN Kin-por Mr Alan LEONG Administration</p>	<p>In reply to Mr LEUNG, the Administration clarified that –</p> <ul style="list-style-type: none"> (a) as defined under the Insurance Companies Ordinance (Cap. 41) ("ICO"), captive insurers were insurers carried on general business only (i.e. non-life insurance), and were restricted to the insurance and reinsurance of risks of "companies within the same grouping of companies"; (b) captive insurers incorporated in Hong Kong and authorized to conduct captive insurance business under ICO would be eligible for the proposed tax concession; and (c) assessable profits of an authorized captive insurer would be ascertained by a formula specified in the amended section 23A of IRO (Clause 6 of the Bill). <p>Mr LEUNG considered that the proposed profits tax rate at 8.25% (i.e. one-half of the normal tax rate of the current 16.5% for corporations) was not competitive enough, and said that he might consider moving Committee Stage amendments to exempt captive insurers from profits tax in the first two years of their operation in Hong Kong.</p> <p>Mr CHAN opined that the Administration should consider exempting captive insurers from all profits tax, taking into account the potential economic benefits (e.g. creation of jobs for related businesses) brought by the development of captive insurance in Hong Kong.</p> <p>Mr LEONG said that Members belonging to the Civic Party took the view that the Administration should consider offering tax concessions of a greater magnitude in</p>	

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		<p>enhancing Hong Kong's competitiveness to captive insurers vis-à-vis other jurisdictions which had offered higher concessionary rates for a number of years.</p> <p>The Administration said that -</p> <p>(a) the current proposal was only a first step to attract enterprises to set up captive insurers in Hong Kong and the Administration would keep in view developments in considering whether further measures were necessary in future; and</p> <p>(b) the insurance industry considered that, with a robust legal and regulatory regime, Hong Kong had the potential to become a domicile for captive insurers. With its proximate location to the Mainland, Hong Kong would also benefit from the anticipated growth in the use of captive insurance by Mainland enterprises.</p> <p>At the request of the Chairman, the Administration agreed to provide a written response to members' suggestions above.</p>	<p>The Administration to take action as per paragraph 7(e) of the minutes.</p>
004228 – 004611	Chairman Mr CHAN Kam-lam Administration	<p>Mr CHAN considered that the current maximum relevant income level of \$30,000 under the Mandatory Provident Fund ("MPF") Schemes Ordinance (Cap. 485) should not be increased further so as to avoid imposing more financial burden on the middle class in making MPF contributions.</p> <p>The Chairman said that Mr CHAN's views were not directly related to the Bill.</p>	
004612 – 004934	Chairman Mr Kenneth LEUNG Administration	<p>Mr LEUNG stressed that, while granting profits tax exemption to captive insurers would have an impact on tax revenue in the short term, attracting more captive insurers to domicile in Hong Kong would provide more business opportunities for Hong Kong and ultimately bring more tax revenue in the medium to long term.</p>	

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		In reply to Mr LEUNG, the Administration advised that it was studying the taxation issues, including treatment of losses, after transfer of assets and liabilities in mergers to be effected under the new Companies Ordinance ("CO") (Cap. 622), and would inform the industry and other stakeholders of the outcome.	
004935 – 005005	Chairman	Members agreed that it was not necessary to invite the public or relevant parties to give views on the Bill.	
<u>Clause by Clause Examination of the Bill</u>			
005006 – 005834	Chairman Administration Assistant Legal Adviser 2 ("ALA2")	<p>Part 1</p> <p>Preliminary</p> <p><u>Clause 1 – Short title</u></p> <p><u>Clause 2 – Inland Revenue Ordinance amended</u></p> <p>Part 2</p> <p>Amendments regarding Profits Tax Concession for Qualifying Captive Insurance Business</p> <p><u>Clause 3 – Application</u></p> <p><u>Clause 4 – Section 14B amended (qualifying reinsurance business)</u></p> <p><u>Clause 5 – Section 19CA amended (treatment of losses: concessionary trading receipts)</u></p> <p><u>Clause 6 – Section 23A amended (ascertainment of assessable profits of insurance corporations other than life insurance corporations)</u></p> <p>In reply to ALA2, the Administration clarified that "premiums from insurance of offshore risks" received by an authorized captive insurer <u>included reinsurance</u> (and not just insurance) underwritten by the captive insurer for the same grouping of companies to which it belonged.</p>	

Time Marker	Speaker	Subject(s)	Action Required
005835 – 010817	Mr James TO Mr Kenneth LEUNG Chairman Administration	<p>In reply to Mr TO, the Administration advised that the definition of captive insurer was provided in section 2(7) of ICO to mean an insurer which carried on general business only and such business was restricted to underwriting insurance and reinsurance of risks of companies within the same grouping of companies to which the captive insurer belonged. The definition of "same grouping of companies" had the meaning assigned to it under CO to include associated companies. It might cover a company which the captive insurer or any company belonging to the same group held, or was entitled to control the exercise of; not less than 20% of the voting power at any general meeting.</p> <p>Mr TO considered the percentage of controlling stake (i.e. not less than 20%) in question might be over generous for the purpose of the proposed tax concession in view of the implications on tax revenue.</p> <p>The Chairman reiterated members' views that the economic benefits of the proposal should be taken into account although there would be reduction in profits tax revenue in the short term.</p> <p>At the request of the Chairman, the Administration agreed to provide a written response to Mr TO's views above, including providing the definition of "same grouping of companies" or other relevant definitions adopted by other jurisdictions for similar purpose.</p>	The Administration to take actions as per paragraph 8(a) and (b) of the minutes.
010818 – 011142	Mr James TO Chairman Administration	<p>In reply to Mr TO about the definition of "offshore risks", the Administration advised that a definition on "premiums from insurance of offshore risks" would be added to section 23A(3) of IRO under clause 6 (5) of the Bill.</p> <p>At the request of the Chairman and Mr TO, the Administration agreed to consider the need to provide a definition of "offshore risks" in the Bill.</p>	The Administration to take action as per paragraph 8(c) of the minutes.

Time Marker	Speaker	Subject(s)	Action Required
011143 – 011329	Chairman Administration	<p>Part 3</p> <p>Amendments regarding Maximum Amount Deductible from Assessable Profits or Income for Certain Contributions</p> <p>Division 1—Increase of Maximum Deductible Amount</p> <p><u>Clause 7 – Schedule 3B amended (deduction for the purposes of section 16AA or 26G)</u></p> <p>Division 2—Transitional Provisions</p> <p><u>Clause 8 – Section 89 amended (transitional provisions)</u></p>	
011330 – 012107	Chairman Mr James TO Mr Kenneth LEUNG Administration	<p>Declaration of interests by Mr LEUNG</p> <p>Mr TO enquired whether the Administration had made reference to major tax cases in other jurisdictions involving disputes/loopholes over the scope of "offshore risks" for the purpose of determining profits tax concession to captive insurers.</p> <p>The Administration advised that –</p> <p>(a) the taxation regime of Hong Kong was highly transparent with bilateral comprehensive double taxation agreements signed with 29 jurisdictions which incorporated an Exchange of Information article; and</p> <p>(b) since offshore risks were normally related to offshore profits not subject to Hong Kong taxation, abuses of the proposed tax concession would unlikely arise.</p> <p>At the request of Mr TO and the Chairman, the Administration agreed to provide a written response to Mr TO's enquiry above.</p>	<p>The Administration to take action as per paragraph 8(c) of the minutes.</p>

Time Marker	Speaker	Subject(s)	Action Required
012108 – 012239	Administration Chairman	<p><u>Clause 9 – Schedule 30 added</u></p> <p><i>Schedule 30 – Transitional Provisions Relating to Provisional Salaries Tax and Provisional Profits Tax in respect of Years of Assessment 2014/15 and 2015/16</i></p> <p>In reply to the Chairman's enquiry, the Administration advised that the Inland Revenue Department would compute provisional salaries tax and provisional profits tax based on the taxpayer's entitlement to the increase in deduction ceiling for contributions to recognized retirement schemes for the relevant years of assessment.</p>	
012240 – 013215	Chairman Mr Kenneth LEUNG ALA2 Administration	<p>ALA2 pointed out that the drafting of sections 2(2), 2(4), 4(2) and 4(4) of the proposed Schedule 30 to IRO with regard to the usage of "the ground is..." (English text) and "有關理由是" (Chinese text) was different from that of similar provisions in other parts of IRO (e.g. existing section 3(4) of Schedule 25), and the meaning of these subsections might be not entirely clear when read alone.</p> <p>Mr LEUNG suggested that the subsections under individual sections (i.e. sections 2 and 4) in Schedule 30 could be merged so that it would be clearer to readers what "the ground" was referring to.</p> <p>The Administration advised that it was in line with the plain language initiative of the Department of Justice to avoid unnecessary cross-referencing to enhance simplicity and conciseness of law, such as by adopting a narrative style of drafting. As the subsections in question were not meant to be independent and read alone, the Administration considered that it would be beyond doubt what "the ground" referred to given the narratives established in the respective previous subsections.</p>	The Administration to take action as per paragraph 10 of the minutes.

Time Marker	Speaker	Subject(s)	Action Required
013216 – 013333	Chairman	Completion of scrutiny of the Bill Follow-up arrangements and way forward	

Council Business Division 1
Legislative Council Secretariat
16 April 2014